1 Executive summary

Overview

1.1 The UK economy has picked up more strongly in 2013 than we expected in our March forecast. Private consumption and housing investment have surprised on the upside, while business investment and net trade have continued to disappoint. Short-term indicators suggest that this momentum has been maintained into the final quarter of the year, leading us to revise up our forecast for GDP growth in 2013 as a whole from 0.6 per cent to 1.4 per cent. We judge the positive growth surprise to have been cyclical, reducing the amount of spare capacity in the economy, rather than indicating stronger underlying growth potential.

1.2 We do not expect the quarterly growth rates seen during 2013 to be sustained in 2014. While consumer confidence, credit conditions and the housing market have improved, productivity and real earnings growth have remained weak. Ultimately, productivity-driven growth in real earnings is necessary to sustain the recovery. So we expect quarterly GDP growth to slow into 2014, and then to strengthen gradually as productivity picks up. The outlook for productivity growth is the key uncertainty confronting all UK forecasters.

1.3 Even though the quarterly growth rates we expect during 2014 are the same as in March, our forecast for growth in 2014 as a whole has risen from 1.8 per cent to 2.4 per cent – simply because the year begins with GDP at a higher level. We expect fractionally weaker growth from 2015 onwards than in March, reflecting weaker exports. Nonetheless, the level of GDP is higher throughout the forecast than in March and we expect the remaining spare capacity in the economy to be absorbed by early 2019 – two years earlier than in March.

1.4 Public sector net borrowing (PSNB) – the gap between what the Government spends and raises in revenue – is forecast to be £111.2 billion this year (measured on an underlying basis, excluding transfers related to the Royal Mail Pension Plan and quantitative easing). This is £8.6 billion lower than our March forecast and £3.8 billion lower than in 2012-13.

1.5 We have revised our receipts forecast for this year up by £3.4 billion (excluding the effects of borrowing-neutral changes that raise both receipts and spending). VAT, onshore corporation tax and stamp duty are all expected to out-perform our March forecast. We have revised spending down by £5.2 billion on the same basis. This largely reflects the fact that we expect central government departments to underspend the Treasury limits they faced in March by £7 billion, rather than the £3.5 billion we forecast at the time. The Treasury has cut the central reserve against those limits by £2 billion in the Autumn Statement, presenting that portion of the underspend as a policy measure.

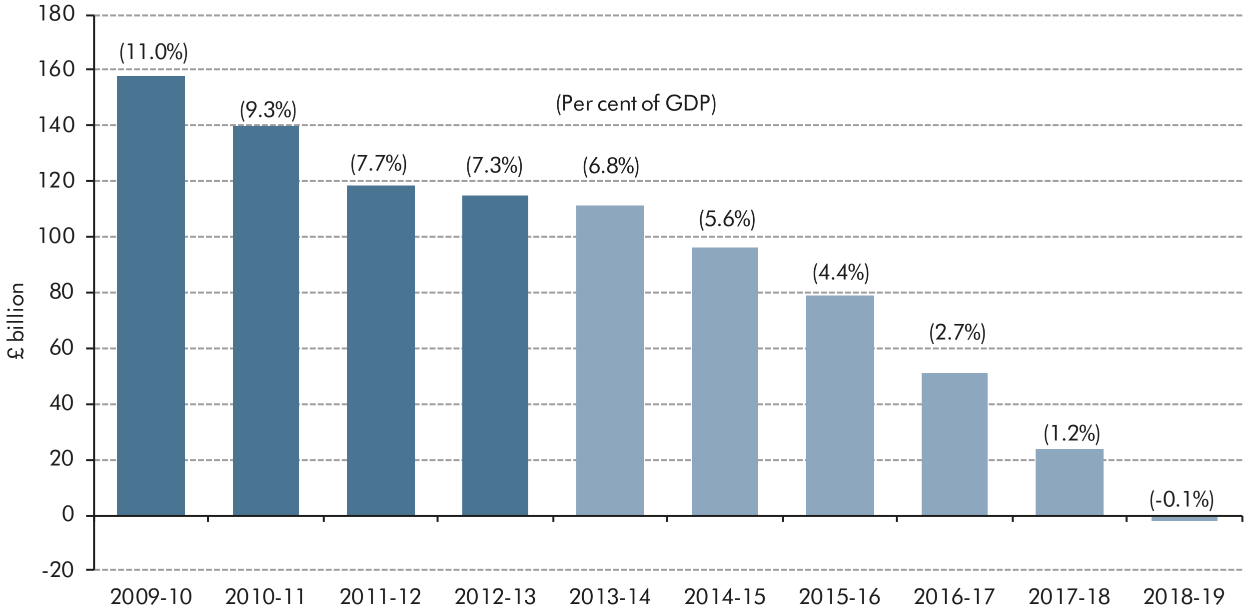
1.6 The downward revisions to our borrowing forecasts increase over time, reaching £19.3 billion in 2017-18, giving a cumulative downward revision of £73.1 billion between 2013-14 and 2017-18. Mirroring our judgement that the upward revision to our economic growth forecast since March is cyclical rather than structural, the downward revisions to our borrowing forecasts reduce the overall budget deficit but not the structural budget deficit.

1.7 Stronger receipts explain the majority of the downward revision to borrowing, with higher profits supporting onshore corporation tax receipts and a stronger property market lifting stamp duty and other capital tax receipts. Our medium-term forecasts for public spending are little changed since March, with a number of factors broadly offsetting each other. In 2018-19, we expect the underlying balance to move into surplus for the first time in 18 years. But the headline balance will still be in modest deficit, as we expect the Treasury to have to find money to transfer to the Bank of England's Asset Purchase Facility.

1.8 The tax and spending measures that the Treasury has included in its Autumn Statement policy decisions table have little cumulative impact on borrowing over the forecast, with the £2 billion cut in departmental spending limits and special reserve this year offsetting a £1.4 billion cumulative net tax cut through to 2018-19 and a £0.6 billion cumulative increase in spending in 2014-15 and 2015-16, the last two years for which detailed departmental spending plans have been set. (This increase in spending comprises £5.5 billion of additional departmental spending, less a £2.2 billion downward 'adjustment', implicitly to other departmental spending, and a £2.7 billion cut in social security and other 'annually managed expenditure'.)

1.9 But there are specific decisions on departmental spending identified in the Autumn Statement policy table that, if continued after 2015-16, would require extra spending between 2016-17 and 2018-19. For example, the extension of free school meals costs £755 million in 2015-16, while the Autumn Statement confirms that removing the cap on student numbers rises to a cost of £720 million by 2018-19. (The size of additional departmental spending pressures was spelt out in detail in the Autumn Statement 2012 and Budget 2013 policy decisions tables, but the Treasury has chosen not to quantify them this time.) This spending would reduce the amount available for departments to spend on other things when plans for those years are set out in future spending reviews. The cost of the net tax cuts in the policy table will also continue to accumulate beyond 2018-19.

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



Source: ONS, OBR

1.10 Our forecast implies that the UK's budget deficit will have fallen by 11.1 per cent of GDP over the nine years from 2009-10 (around £180 billion in today's terms). Around 80 per cent of the reduction is accounted for by lower public spending. This will take government consumption of goods and services – a rough proxy for day-to-day spending on public services and administration – to its smallest share of national income at least since 1948, when comparable National Accounts data are first available. The remaining 20 per cent of the drop in borrowing is accounted for by higher receipts, with the majority having taken place by 2012-13, largely as result of rises in the standard rate of VAT.

1.11 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. In March, we forecast that the CACB would be in surplus by 0.8 per cent of GDP in the then target year of 2017-18. We now expect a slightly smaller surplus of 0.7 per cent of GDP in that year. Thanks to a rise in the average tax rate on national income, and the Government's decision to continue cutting public services spending as a share of GDP, we forecast a bigger surplus of 1.6 per cent of GDP in the new target year of 2018-19, implying significant headroom against the fiscal mandate.

1.12 The Government's supplementary target is for public sector net debt (PSND) to be falling as a share of GDP in 2015-16. But, as in our December 2012 and March 2013 forecasts, we expect PSND still to be rising in that year. We expect PSND to peak at 80.0 per cent of GDP in 2015-16, to fall by a statistically and fiscally insignificant margin in 2016-17, and then to fall more rapidly to 75.9 per cent of GDP by 2018-19. This implies that, relative to the size of the economy, debt will peak at more than double its pre-crisis level.

1.13 Needless to say, there is huge uncertainty around all public finance projections, which increases over longer time horizons. 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 over the coming five years 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

1.14 The economy grew significantly faster over the first three quarters of 2013 than we forecast in March. Cumulative growth was 1.8 per cent over this period, 1.3 percentage points higher than our March forecast. Private consumption grew by 1.6 per cent, 1.4 percentage points higher than our March forecast. Most survey indicators suggest the economy gathered momentum during 2013, although that momentum may have eased slightly in the final months. Inflation has fallen a little more than we expected in March.

1.15 Employment has been higher and unemployment lower than we forecast, continuing the pattern of recent years. The claimant count has fallen particularly rapidly. By contrast, average earnings growth has remained weak. And while GDP has grown far more strongly than we forecast so far this year, the number of hours worked was also higher than expected – productivity per hour grew by just 0.2 per cent over the first three quarters of 2013, weaker even than the modest 0.4 per cent rise we expected in March.

1.16 The housing market has picked up more strongly than forecast this year. House prices increased by 3.8 per cent in the year to September while the volume of property transactions was up 22.6 per cent. So far, this has not translated into strong growth in net mortgage lending. But some forms of credit growth have picked up, in particular car finance, which has supported strong growth in car purchases and contributed to the unexpected strength of private consumption.

The economic outlook

1.17 We have revised up our forecast for growth in 2013 from 0.6 per cent to 1.4 per cent and in 2014 from 1.8 per cent to 2.4 per cent, the latter purely as a consequence of GDP starting the year higher. The main explanation for those upward revisions has been stronger-than-expected private consumption growth in 2013. Residential investment has also grown more strongly than expected. By contrast, business investment and net trade have continued to disappoint. These upward revisions to GDP are broadly in line with those made by external forecasters between March and now.

1.18 We judge the growth surprise in 2013 to have been cyclical, reducing the amount of spare capacity relative to our March forecast, rather than indicating stronger underlying growth potential. As such, we estimate the output gap in the third quarter of 2013 to have been -2.2 per cent of potential output, having narrowed from -2.6 per cent in the fourth quarter of 2012. In March, we expected the output gap to widen over this period. Our output gap forecast is around 1½ percentage points narrower by the end of the forecast period.

1.19 We do not expect the pace of quarterly expansion seen during 2013 to be sustained in 2014. While consumer confidence has recovered, credit conditions have eased and prospects for the housing market have improved, productivity and real earnings growth have remained weak. The unexpected strength of private consumption this year has largely come from lower saving, not higher income. Ultimately, productivity-driven growth in real earnings is necessary to sustain the recovery and raise living standards. We therefore expect quarterly GDP growth to slow into 2014, gradually strengthening thereafter as productivity picks up and real earnings growth provides the foundation for a stronger and more sustained upswing. This recovery in productivity growth is perhaps the most important judgement in our economy forecast. We expect the remaining spare capacity in the economy to be absorbed by early 2019 – two years earlier than we forecast in March.

1.20 We are conscious that forecast revisions tend to lag economic developments at turning points, leading to repeated overestimates of economic activity in downturns and repeated underestimates when activity finally picks up. But the experience of 2010 provides a recent example of what appeared to be a turning point in the cycle ebbing as the factors needed to generate self-sustaining recovery failed to take hold. And with productivity, real income growth and UK export markets remaining weak, and problems in the euro area far from fully resolved, our central forecast – like that of the Bank of England – does not assume that the growth rates seen in the last couple of quarters are maintained through next year and beyond. We assume that growth slows to rates of around 0.5 per cent a quarter through 2014, with risks to both the upside and downside.

1.21 While most public discussion of economic forecasts focuses on real GDP, the key driver of our fiscal forecast is nominal GDP – the cash value of economic activity – and its composition. The level of nominal GDP is higher across the forecast period than in March. That reflects methodological changes to the way in which the ONS calculates nominal GDP, as well as stronger real growth in 2013. Whole economy inflation – as measured by the GDP deflator – is little changed from March. Overall, we forecast nominal GDP to grow by 3.6 per cent in 2013 and to average around 4¼ per cent a year thereafter, with cumulative growth from the end of 2013 unchanged from our March forecast.

1.22 With regards to the composition of nominal GDP:

- in **income** terms: labour income is forecast to grow more slowly than GDP in the near term, despite the strength of employment, as productivity and earnings growth remain subdued. But it picks up from 2015 as productivity growth recovers. Corporate profits have grown faster than GDP this year and are forecast to continue to do so; and

- in **expenditure** terms: private consumption is forecast to grow slightly faster than household income, with the saving ratio falling marginally. Private investment is forecast to recover towards its pre-crisis share of GDP, implying strong growth in business and residential investment for a sustained period. By contrast, the Government's ongoing fiscal consolidation implies large and sustained falls in government consumption of goods and services as a share of GDP, which is projected to reach its lowest level on record in data back to 1948.

Table 1.1: Economic forecast overview

	Percentage change on a year earlier, unless otherwise stated						
	Outturn	Forecast[1]					
	2012	2013	2014	2015	2016	2017	2018
Output at constant market prices							
Gross domestic product (GDP)	0.1	1.4	2.4	2.2	2.6	2.7	2.7
GDP level (2012=100)	100.0	101.4	103.9	106.2	108.9	111.8	114.8
Output gap (per cent of potential output)	-2.6	-2.3	-1.8	-1.6	-1.2	-0.7	-0.2
Expenditure components of GDP at constant market prices							
Household consumption[2]	1.2	1.9	1.9	1.7	2.4	2.8	2.8
Business investment	2.6	-5.5	5.1	8.6	8.7	8.9	7.9
General government consumption	1.7	0.7	0.4	-0.5	-1.0	-1.8	-1.1
General government investment	4.6	-6.9	7.3	1.2	2.1	0.5	-1.1
Net trade[3]	-0.7	-0.2	0.0	0.1	0.0	0.0	-0.1
Inflation							
CPI	2.8	2.6	2.3	2.1	2.0	2.0	2.0
Labour market							
Employment (millions)	29.5	29.9	30.2	30.4	30.7	30.9	31.2
Average earnings[4]	2.0	1.5	2.6	3.3	3.5	3.7	3.8
ILO unemployment (% rate)	7.9	7.6	7.1	7.0	6.6	6.1	5.6
Claimant count (millions)	1.59	1.43	1.27	1.23	1.18	1.13	1.10
	Changes since March forecast						
Output at constant market prices							
Gross domestic product (GDP)	0.0	0.8	0.6	-0.1	-0.1	-0.1	
GDP level (2012=100)[5]	0.0	0.8	1.4	1.3	1.2	1.1	
Output gap (per cent of potential output)	0.1	1.2	1.9	1.8	1.7	1.6	
Expenditure components of GDP at constant market prices							
Household consumption[2]	0.2	1.5	0.7	0.0	0.0	0.0	
Business investment	-2.3	-7.4	-1.0	0.0	0.1	0.3	
General government consumption	-0.9	0.3	1.1	-0.1	0.0	0.0	
General government investment	1.9	-9.5	2.4	-0.7	3.6	1.7	
Net trade[3]	0.1	-0.3	-0.1	-0.1	-0.1	-0.1	
Inflation							
CPI	0.0	-0.2	-0.1	0.0	0.0	0.0	
Labour market							
Employment (millions)	0.0	0.1	0.3	0.3	0.4	0.4	
Average earnings[4]	0.0	0.0	-0.2	-0.4	-0.4	-0.3	
ILO unemployment (% rate)	0.0	-0.3	-0.9	-0.9	-0.9	-0.8	
Claimant count (millions)	0.00	-0.15	-0.36	-0.35	-0.30	-0.24	

[1] The forecast is consistent with the second estimate of GDP data for the third quarter of 2013, released by the Office for National Statistics on 27 November 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 March.

1.23 We have revised up our employment forecast, with total employment expected to reach 31.2 million in 2018. Unemployment is forecast to fall steadily over the coming years, reaching 7 per cent in mid-2015 and 6 per cent by the end of 2017. The path of unemployment is lower than we forecast in March, reflecting lower-than-expected unemployment this year carrying through to the rest of the forecast.

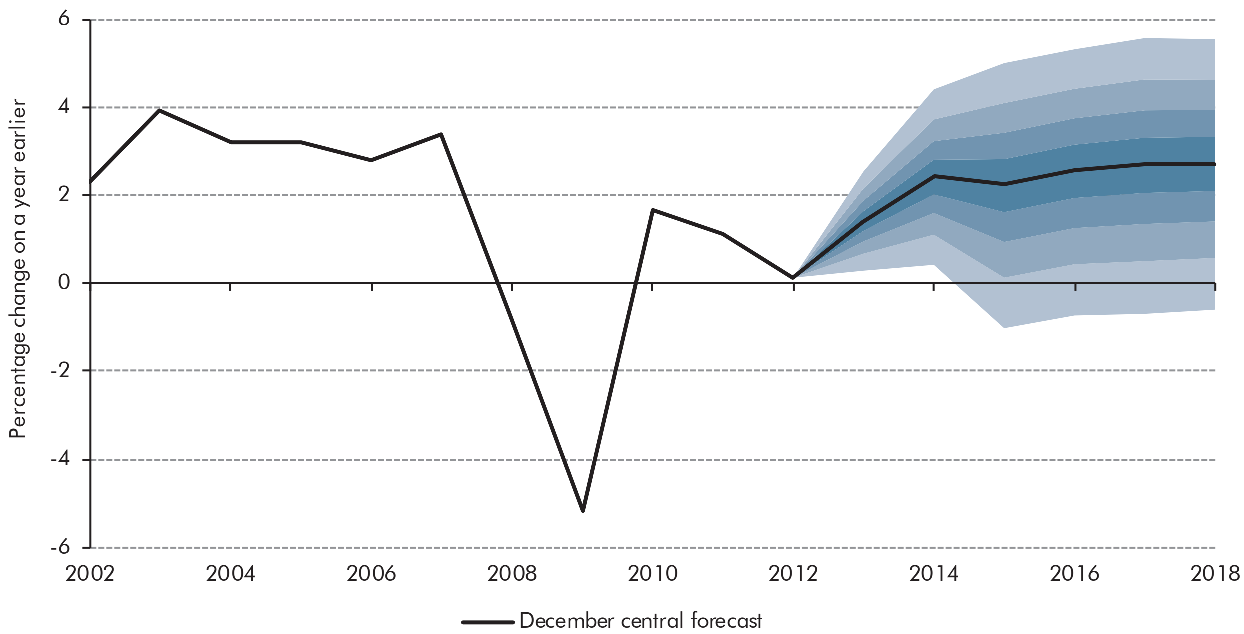
1.24 Total market sector employment is forecast to rise by 3.1 million between the start of 2011, the beginning of the period covered by the Government's 2010 Spending Review, and the start of 2019. This more than offsets a 1.1 million fall in general government employment.

1.25 With CPI inflation having fallen back more than expected, our forecast is slightly lower in the near term than it was in March. Currently at 2.2 per cent, CPI inflation is forecast to fall back to the Bank of England's 2 per cent target during 2016. Relative to our March forecast, the extra downward pressure on inflation from a slightly stronger exchange rate broadly offsets the reduced downward pressure from spare capacity in the economy.

1.26 Our house price inflation forecast has been revised up significantly, reflecting the momentum in house prices this year and supportive mortgage financing conditions. We expect house price inflation to be above 5 per cent in 2014 and 7 per cent in 2015. Relative to our March forecast, we have revised the level of house prices up 10 per cent by 2017-18.

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 forecast 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 5 per cent chance that the economy will shrink in 2014 and a similar chance it will grow by more than 5 per cent.

Chart 1.2: Real GDP growth fan chart



Source: ONS, OBR

The fiscal outlook

1.28 The headline public finance measures have been affected by a number of one-off or temporary factors in recent years. Two of these have had large effects on borrowing – the one-off transfer of the Royal Mail Pension Plan's assets (and associated future pension liabilities) to the Government in 2012-13 and the ongoing transfers of cash from the Asset Purchase Facility (APF) to the Exchequer. We focus our assessment of the public finances on an underlying measure of public sector net borrowing ('underlying PSNB') that excludes these two factors. Headline ONS measures are also presented.

1.29 Underlying PSNB is estimated to have fallen by around a third between 2009-10 and 2012-13. The pace of deficit reduction slowed in 2012-13, reflecting weak growth and the delayed impact on the public finances of high inflation in the previous year. We expect another relatively modest decline this year. Table 1.2 shows that we forecast the deficit to fall more rapidly over the next five years, reaching a small surplus in 2018-19. Headline borrowing remains in modest deficit in 2018-19, as we assume that the Government will have to borrow to fund transfers from the Exchequer to the APF as quantitative easing unwinds.

1.30 As set out above, we judge the unexpected strength of real GDP growth this year to have been cyclical and so we have not changed our view of the economy's underlying supply potential. This judgement means that our estimate of the structural position of the public finances – cyclically-adjusted PSNB – is little changed from March, with the downward revisions to unadjusted borrowing judged to be cyclical.

Table 1.2: Fiscal forecast overview

	Per cent of GDP						
	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Underlying fiscal aggregates							
Public sector net borrowing[1]	7.3	6.8	5.6	4.4	2.7	1.2	-0.1
Cyclically-adjusted net borrowing[1]	5.5	5.2	4.3	3.3	1.9	0.7	-0.3
Surplus on current budget[1]	-5.9	-5.3	-4.0	-2.9	-1.2	0.2	1.4
Headline fiscal aggregates							
Public sector net borrowing	5.1	6.0	4.9	4.0	2.6	1.3	0.1
Cyclically-adjusted net borrowing	3.3	4.4	3.6	2.9	1.7	0.8	-0.1
Surplus on current budget	-5.5	-4.5	-3.3	-2.5	-1.1	0.2	1.4
Fiscal mandate and supplementary target							
Cyclically-adjusted surplus on current budget	-3.6	-2.9	-2.0	-1.4	-0.2	0.7	1.6
Public sector net debt	73.9	75.5	78.3	80.0	79.9	78.4	75.9
	Changes since March forecast						
Public sector net borrowing[1]	-0.5	-0.7	-0.9	-1.1	-1.0	-1.1	
Cyclically-adjusted net borrowing[1]	-0.4	0.1	0.3	0.1	0.2	0.0	
Surplus on current budget[1]	0.5	0.7	0.9	1.1	1.1	1.1	
Cyclically-adjusted surplus on current budget	0.4	-0.1	-0.3	-0.2	-0.3	-0.1	
Public sector net debt	-2.0	-3.6	-4.3	-5.1	-5.7	-6.4	

[1] Excluding Royal Mail and APF transfers.

1.31 Table 1.3 shows that we have reduced our forecast for the underlying deficit in 2013-14 by £8.6 billion, due to stronger-than-expected receipts and a forecast of larger-than-expected underspending by departments. Excluding borrowing-neutral changes that have raised both receipts and annually managed expenditure (AME) since March, receipts have been revised up by £3.4 billion in 2013-14. VAT, onshore corporation tax and stamp duty are all expected to out-perform our March forecast by more than £1 billion. We have revised spending down by £5.2 billion on the same underlying basis. This largely reflects the fact that we expect government departments to underspend the Treasury limits they faced in March by £7 billion, rather than the £3.5 billion we forecast at the time. The Treasury has cut the central reserve against those limits by £2 billion in the Autumn Statement, presenting that portion of the underspend as a policy measure. The underlying deficit is expected to fall by £3.8 billion between 2012-13 and 2013-14, compared to £3.5 billion in the previous year and a more rapid average decline of £19.7 billion over the previous two years.

1.32 The downward revisions to our borrowing forecasts increase over time, reaching £19.3 billion in 2017-18. This gives a cumulative reduction in our underlying borrowing forecasts of £73.1 billion since March between 2013-14 and 2017-18. Stronger receipts explain the majority of that change, with higher profits supporting onshore corporation tax receipts and a stronger property market lifting stamp duty and other capital tax receipts. Our forecasts for public spending are little changed since March, with a number of factors largely offsetting each other. However, these factors increase our AME forecast, reducing the implied amount available for departmental spending on public services and administration and on investment.

Table 1.3: Change in underlying public sector net borrowing

	£ billion						
	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Public sector net borrowing[1]							
March forecast	120.9	119.8	108.4	95.5	67.0	42.7	
December forecast	115.0	111.2	96.0	78.7	51.1	23.4	-2.2
Change	**-5.9**	**-8.6**	**-12.4**	**-16.8**	**-15.9**	**-19.3**	
of which:							
Pre-measures forecasts							
of which:							
Receipts[1,2]	-4.3	-3.4	-9.6	-13.2	-14.5	-14.6	
DEL spending[3]	-0.5	-1.8	0.0	-1.3	0.3	-4.0	
AME spending[1,2,3]	-1.1	-1.4	-2.9	-2.4	-2.1	-1.3	
Measures in the Treasury's policy decision table	0.0	-2.0	0.1	0.1	0.4	0.6	

[1] Excluding Royal Mail and APF transfers.

[2] Excluding fiscally neutral switches, which include changes in the proportion of tax credits treated as negative tax, Renewables Obligation and the treatment of artistic originals in public corporations' gross operating surplus and capital expenditure.

[3] DEL and AME have been adjusted to remove the effects of the OSCAR classification changes on DEL, which are largely offset in AME, explained in Box 4.4.

1.33 Our forecast suggests that underlying net borrowing will have fallen by 11.1 per cent of GDP over the nine years from 2009-10 (around £180 billion in today's terms), taking it from its post-war peak to what would be the first budget surplus since 2000-01. On our central forecast, as Chart 1.3 shows, the contributions to this would be:

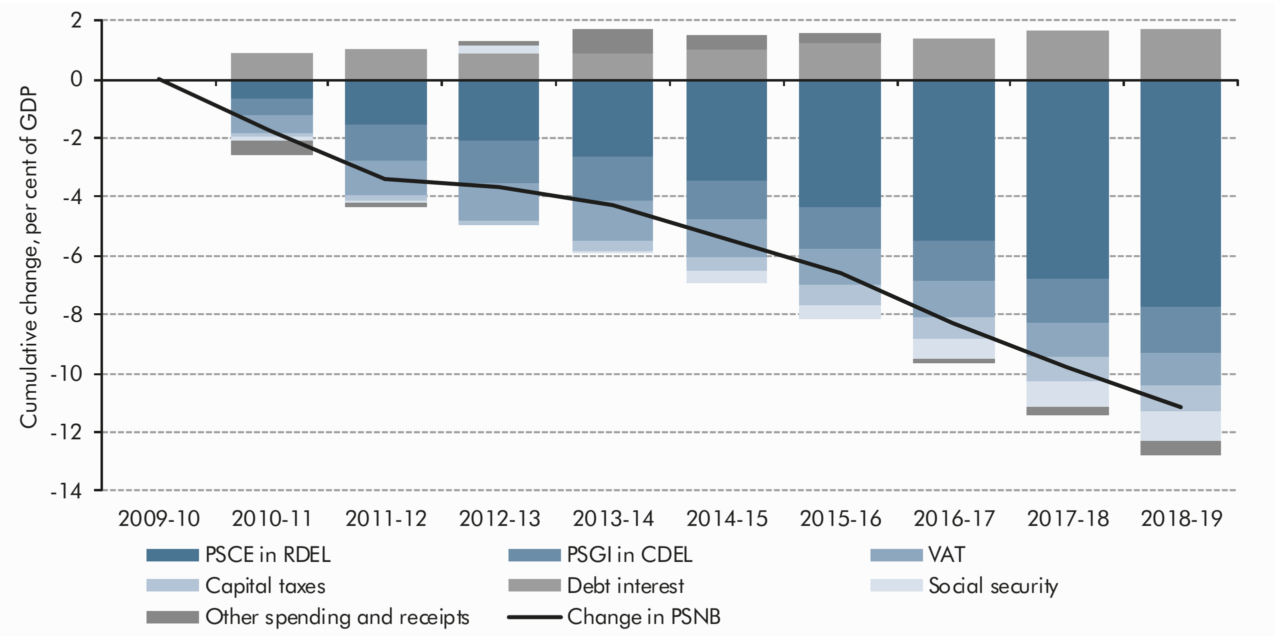
- 8.8 per cent of GDP, or around 80 per cent of the deficit reduction, from lower expenditure, with Total Managed Expenditure falling from 47.1 per cent of GDP in 2009-10 to 38.2 per cent of GDP by 2018-19. Within this total:[1]
  - PSCE in RDEL, a proxy for day-to-day spending on public services and administration, falls by 7.8 per cent of GDP to 14.2 per cent in 2018-19. This is mirrored in our GDP forecast, where government consumption of goods and services falls from 23.2 per cent of nominal GDP in 2009 to 16.1 per cent by the end of the forecast period, its lowest on record in data back to 1948;
  - PSGI in CDEL, a measure of public sector investment, falls by 1.6 per cent of GDP to 1.9 per cent in 2018-19. In 2007-08, PSGI in CDEL was 2.6 per cent of GDP; and

[1] We have adjusted spending figures in outturn for significant spending-neutral switches between DEL and AME.

   - social security spending falls by 1.0 per cent of GDP to 10.0 per cent in 2018-19 – still higher than its pre-crisis level.

- 2.3 per cent of GDP, or around 20 per cent of the deficit reduction, from higher receipts, with the majority of the increase having taken place by 2012-13, largely as a result of the increases in the standard rate of VAT. This is followed by further increases towards the end of our forecast due to the resumption of fiscal drag, as above-inflation earnings growth pushes more income into higher tax brackets.

Chart 1.3: Sources of deficit reduction



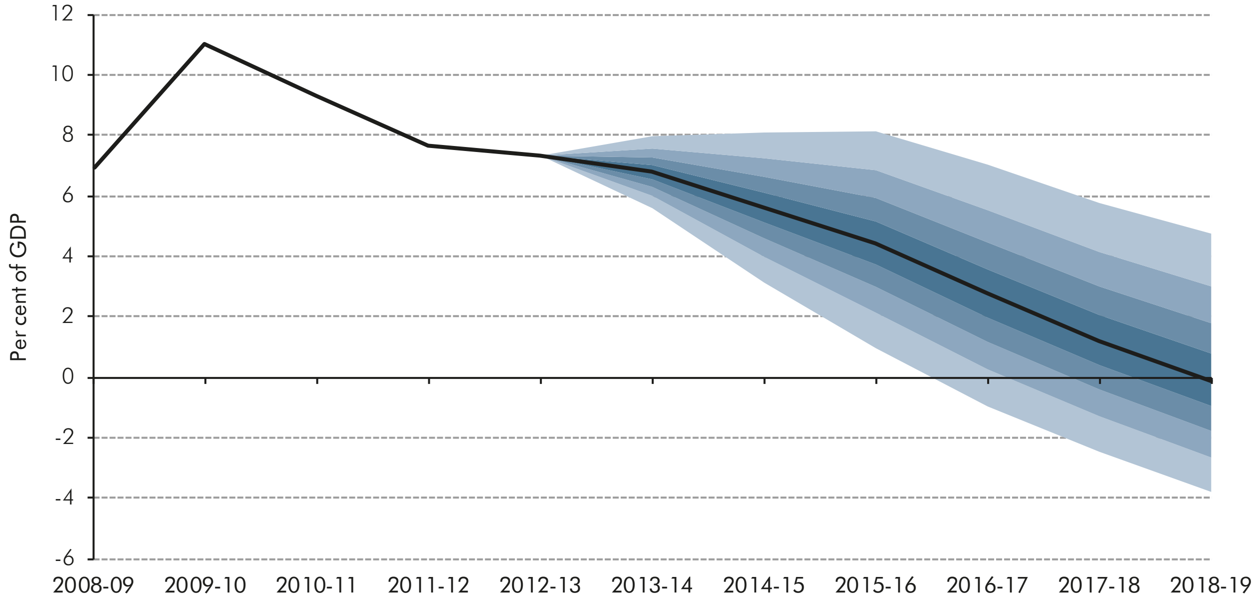
Source: ONS, OBR. Excludes Royal Mail and APF transfers. See paragraph 4.162.

1.34 The current budget balance, which excludes borrowing to finance net investment spending, is forecast to show a deficit of £74.2 billion this year (£86.3 billion on an underlying basis), down from a peak of £109.5 billion in 2009-10. The current balance moves into surplus in 2017-18 and records a surplus of £28.0 billion in 2018-19. With planned investment spending little changed, revisions to the current balance are similar to those to PSNB.

1.35 The cyclically-adjusted current budget (CACB) moves from a deficit of 2.9 per cent of GDP in 2013-14 to a surplus of 1.6 per cent of GDP in 2018-19. We expect the CACB to move into surplus in 2017-18. As with cyclically-adjusted PSNB, there have been relatively small revisions to the CACB as we judge the improvement in the current balance to be largely cyclical rather than structural.

1.36 All forecasts are subject to significant uncertainty. Chart 1.4 shows our median forecast for underlying 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 forecast errors were to be a reasonable guide to future forecast errors.

Chart 1.4: Underlying PSNB fan chart



Source: ONS, OBR. Excludes Royal Mail pension fund and APF transfers

1.37 We forecast public sector net debt (PSND) to rise as a share of GDP in each year up to and including 2015-16, peaking at 80.0 per cent of GDP. It falls by a statistically and fiscally insignificant margin in 2016-17, and more rapidly thereafter, reaching 75.9 per cent of GDP in 2018-19. PSND in 2017-18 is now forecast to be 6.4 per cent of GDP lower than we forecast in March. Table 1.4 breaks this change down as follows:

- nominal GDP was revised up by around 1.3 per cent in Blue Book 2013, due largely to methodological changes. Combined with changes to our nominal GDP forecast, this reduces the ratio of the cash value of debt to GDP by 2.3 per cent of GDP in the peak year of 2015-16 and by 2.2 per cent in 2017-18; and

- our forecast for PSND in cash terms is £51 billion lower in 2015-16 and £82 billion lower in 2017-18 than in March, which is largely due to lower cumulative net borrowing over the forecast period. This reduces PSND by 2.8 per cent of GDP in 2015-16 and 4.2 per cent in 2017-18.

Table 1.4: Change in public sector net debt

	Per cent of GDP					
	Outturn	Forecast				
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
March forecast	75.9	79.2	82.6	85.1	85.6	84.8
December forecast	73.9	75.5	78.3	80.0	79.9	78.4
Change	**-2.0**	**-3.6**	**-4.3**	**-5.1**	**-5.7**	**-6.4**
of which:						
Change in nominal GDP[1]	-1.5	-2.6	-2.4	-2.3	-2.3	-2.2
Change in cash level of net debt	-0.4	-1.0	-1.9	-2.8	-3.4	-4.2
	£ billion					
March forecast	1189	1286	1398	1502	1580	1637
December forecast	1182	1269	1365	1451	1515	1554
Change in cash level of net debt	**-7**	**-18**	**-33**	**-51**	**-65**	**-82**
of which:						
Changes in net borrowing	-6	-15	-28	-43	-56	-74
Financial transactions and other	-1	-3	-5	-7	-9	-9

[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 2018-19; and
- to see public sector net debt (PSND) falling as a share of GDP in 2015-16.

1.39 We judge that the Government has a greater than 50 per cent chance of meeting the fiscal mandate. The CACB is forecast to be in surplus by 1.6 per cent of GDP in 2018-19, the first surplus in excess of 1 per cent of GDP we have forecast for a mandate year.

1.40 PSND is forecast to rise to a peak of 80.0 per cent of GDP in 2015-16, which is slightly lower and a year earlier than we forecast in March. However, as in March, our forecast does not show the Government on course to achieve the supplementary target – we forecast that debt will rise by 1.7 per cent of GDP in the target year, down from an increase of 2.4 per cent of GDP in our March forecast.

1.41 There is considerable uncertainty around our central forecast. 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 test 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 80 per cent probability that the CACB will be in balance or surplus in 2018-19 (as the mandate requires) and a roughly 65 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 relates to our estimates of future potential output. If potential output is lower than we estimate, reducing the size of the output gap in the target year, the structural portion of borrowing would be larger. If potential output was 1 per cent lower than in our central forecast in 2018-19, the probability of meeting the mandate would fall to 70 per cent; and
- third, by looking at alternative economic scenarios. We have looked at four scenarios for the pace at which unemployment falls back to the 7 per cent threshold in the Bank of England's monetary policy forward guidance – reaching the threshold either a year earlier or a year later than in the central forecast. Unemployment could fall faster than expected for good reasons – stronger demand – or bad reasons – lower potential output. Equally, it could fall more slowly than expected for good reasons – higher potential output – or bad reasons – weaker demand. The Government would continue to meet the fiscal mandate in all scenarios, reflecting the substantial CACB surplus in 2018-19 in our central forecast. The supplementary debt target would be missed in all scenarios. The most challenging of the scenarios is that where unemployment falls more rapidly than expected due to lower potential output implying less scope for the economy to grow before spare capacity has been fully absorbed.