

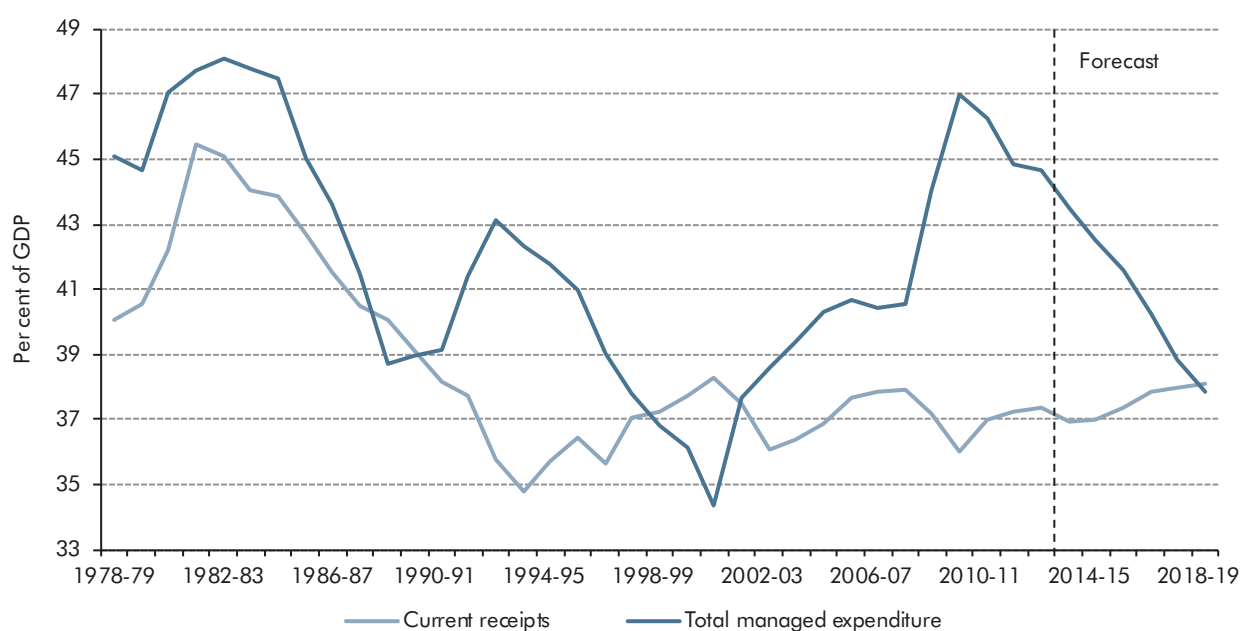
1 Executive summary

Overview

- 1.1 The UK economy has continued to recover. In the final quarter of 2013, GDP growth matched our December forecast, inflation fell back to target and unemployment dropped more quickly than expected. But productivity and wage growth remained disappointing.
- 1.2 Revised data published since our last forecast suggest the economy grew slightly faster over 2013 as a whole than we expected in December, with GDP up 1.8 per cent on the previous year. Consumer spending, supported by a falling saving ratio, has been the biggest driver of recent growth, while the latest data suggest business investment is recovering. Housing market indicators have picked up sharply, but export performance remains disappointing.
- 1.3 Given the momentum the economy carried into 2014, we have revised our GDP growth forecast up slightly to 2.7 per cent in 2014 and 2.3 per cent in 2015. We expect quarterly growth rates to ease through 2014 as consumer spending growth slows to rates more aligned with household income growth. The outlook for productivity growth, which underpins income growth and the sustainability of the recovery, remains the key uncertainty. We expect inflation to remain close to target and unemployment to continue falling in the coming years, though at a slower pace than in recent months.
- 1.4 We estimate that activity in the economy was 1.7 per cent below its sustainable potential level at the end of 2013, a slightly narrower output gap than in our December forecast. This is consistent with the unexpectedly large fall in the unemployment rate to 7.2 per cent in the fourth quarter. Combining this narrower output gap with a slightly stronger GDP growth forecast, we now expect the economy to return to normal capacity and the output gap to close by mid-2018, around a year earlier than forecast in December.
- 1.5 Public sector net borrowing (PSNB) – the gap between what the Government spends and raises in revenue – is expected to be £107.8 billion this year (measured on an underlying basis, excluding transfers related to the Royal Mail Pension Plan and quantitative easing). This is £3.4 billion lower than our December forecast and £7.0 billion lower than in 2012-13. Borrowing is forecast to fall by a further £12.4 billion in 2014-15, to £95.5 billion, moving below £100 billion for the first time in six years. The largest drivers of our downward revisions to borrowing in 2013-14 are an upward revision to stamp duty receipts (due to higher house prices and property transactions) and a downward revision to debt interest costs (due to lower inflation). But borrowing in 2014-15 is little changed from our December forecast, in part because we expect social security spending to be higher and because stronger growth in the UK is expected to raise EU contributions in that year (an effect we expect to unwind in the future due to the UK rebate).

- 1.6 We have revised borrowing lower in each subsequent year of the forecast, reflecting stronger receipts in every year and slightly lower spending from 2015-16, including the effects of policy measures. The downward revision averages almost £6 billion a year from 2015-16 to 2017-18, before falling to £2.6 billion in 2018-19. The improvement in 2018-19 is smaller because of slower GDP and employment growth, once the output gap has closed, and the Government's assumption that it will raise total public spending in line with whole economy inflation in that year, the forecast for which we have revised higher since December. In 2018-19, we forecast the public finances to move into surplus for the first time in 18 years.
- 1.7 The tax and spending measures that the Treasury has included in its Budget policy decisions table have little cumulative effect on borrowing over the forecast, with a £5½ billion cumulative net tax cut offset by a £5¾ billion cumulative reduction in spending. The net tax cut reflects the partly offsetting effects of a number of measures that reduce receipts – including raising the income tax personal allowance, the package of savings measures and the temporary increase in the annual investment allowance to £500,000 – and others that increase receipts – including accelerated payments in anti-avoidance cases and the income tax associated with more flexible access to pension assets. Spending cuts are focused in the years from 2016-17 to 2018-19, for which detailed plans have not yet been set. The Government has also made spending commitments related to energy intensive industries in this Budget that it estimates will cost around £0.5 billion a year from 2016-17.
- 1.8 A number of measures have markedly different implications for revenue beyond the 5-year scorecard period than within it. These include: the pension withdrawals measure, which brings forward income tax receipts but has a small steady-state cost in the long term; voluntary NICs, which increases NICs receipts in the short term but also increases long-term state pension costs; the temporary annual investment allowance increase, which raises the amount of tax relief that can be claimed until December 2015, but then reduces it thereafter, largely recouping the scorecard costs; and accelerated payments related to tax avoidance schemes, which brings forward receipts from future years.
- 1.9 The net effect of these measures is to increase receipts over the scorecard horizon by £1.2 billion a year on average, but the revenue raised then drops sharply in 2019-20 and averages only £0.2 billion a year over the 15 years beyond the scorecard period. Given the uncertainty associated with costing these policy measures over a 5-year horizon, the longer-term implications will be also be subject to considerable uncertainty.
- 1.10 Our forecast implies that by 2018-19 the UK's budget deficit will have fallen by 11.2 per cent of GDP from its post-war peak in 2009-10 (around £190 billion in today's terms). Just over 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. Just under 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.

Chart 1.1: Total public sector spending and receipts



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

- 1.11** The Government's 'fiscal mandate' requires it to balance the cyclically-adjusted current budget (CACB) – the amount the Government has to borrow to finance non-investment spending, adjusted for the state of the economy – five years ahead. In December, we forecast that the CACB would be in surplus by 1.6 per cent of GDP in 2018-19. We now forecast the surplus in 2018-19 to be 1.5 per cent of GDP, fractionally less than we forecast in December. This reflects the net effect of lower assumed spending beyond the current Spending Review period, including the further spending reductions from Budget policy measures in that year, and receipts being slightly lower as a share of GDP despite a narrower output gap.
- 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. As in each forecast we have produced since December 2012, we expect PSND still to be rising in that year. We now expect PSND to peak at 78.7 per cent of GDP in 2015-16, to fall by a small margin in 2016-17 and then to fall more rapidly to 74.2 per cent of GDP by 2018-19. Debt as a share of GDP is lower in each year of our forecast than in December, reflecting lower borrowing and upward revisions to our nominal GDP forecast.
- 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 GDP growth in the fourth quarter of 2013 was in line with our December forecast at 0.7 per cent. Revised data suggest growth in the first half of the year was stronger than previously estimated, so growth in the year as a whole was 1.8 per cent, a little faster than the 1.4 per cent we forecast in December. Consumer spending was the main driver of growth in 2013, with lower saving playing a bigger role than higher incomes in financing the rise in spending through the year. Revised data now suggest that business investment picked up in 2013, rising 8.5 per cent in the year to the final quarter – although further revisions are highly likely. Inflation fell a little more than we expected, with the latest rate below the Bank of England's inflation target of 2 per cent for the first time since late 2009.
- 1.15 Despite the forecast revisions we made in December, labour market data continued to surprise us with lower unemployment, higher employment and lower wage growth than we had expected in the final quarter of 2013. Productivity growth remains very weak. Output per hour was just 0.2 per cent higher in the second half of 2013 than in the first half.
- 1.16 Housing market indicators accelerated. House prices increased 5.5 per cent in the final quarter of the year on the ONS measure, with lenders' price indices showing some sharp monthly increases so far this year. Mortgage approvals point to continued growth in activity, rising by 42 per cent in the year to January. There are also signs of this feeding through to construction, with housing starts up 33 per cent in the year to mid-2013. But reports of shortages in building materials and skilled labour suggest the housing supply response may be constrained in the short term.

The economic outlook

- 1.17 Given the momentum the economy carried into 2014, we have revised up our forecast for GDP growth in 2014 by 0.3 percentage points to 2.7 per cent, in line with the average of outside forecasts, and in 2015 by 0.1 percentage points to 2.3 per cent, slightly below the outside average. The largest source of upward revision in 2014 is business investment, following further extensive revisions to 2013 data.
- 1.18 Consumer spending increased faster than household disposable incomes in 2013, reducing the saving ratio to an estimated 5.0 per cent from 7.2 per cent in 2012. We expect consumption growth to slow to rates more aligned with household income growth during 2014. However, income growth should be boosted by a recovery in productivity growth, though employment growth is expected to slow from recent high rates.
- 1.19 Unemployment fell to 7.2 per cent in the final quarter of 2013, 0.2 percentage points below our December forecast. Partly reflecting this, we estimate the output gap to have been -1.7 per cent of GDP in that quarter, 0.2 percentage points narrower than our December estimate. We continue to judge that much of the recovery in 2013 can be attributed to stronger demand that was not accompanied by improved underlying supply potential. That judgement is supported by weak productivity growth, tighter labour market conditions and the fall in the saving ratio.

- 1.20 The combination of a slightly stronger near-term outlook for GDP growth and a slightly narrower output gap than forecast in December means the output gap is now expected to close by mid-2018, around a year earlier than in our December forecast. Since we assume that growth will be in line with its trend rate once the output gap has closed, rather than forecasting further cyclical fluctuations around that trend, we have revised our GDP growth forecast in 2018 down slightly to 2.5 per cent.
- 1.21 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 growth, real income growth and UK export markets remaining weak, and risks in the euro area and emerging markets remaining, our central forecast assumes that growth slows to rates of around 0.6 per cent a quarter through 2014 and 2015, with risks to both the upside and downside.
- 1.22 While most 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. This reflects developments in real GDP and whole economy inflation. Nominal GDP is higher across the forecast than in December. That mainly reflects stronger than expected nominal GDP growth in the final quarter of 2013 and slightly higher expected GDP deflator growth looking forward, thanks to a change in the way we forecast the private consumption deflator. Overall, we forecast nominal GDP to grow by 5.0 per cent in 2014, to dip to 4.0 per cent in 2015 and to average around 4½ per cent a year thereafter. The dip in 2015 is explained by strong growth in the second half of 2013 lifting the 2014 annual average growth rate, rather than an expectation that quarterly growth rates will slow in 2015.
- 1.23 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, as employment growth slows and 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 a little further. 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 since comparable records began in 1948.

Table 1.1: Economic forecast overview

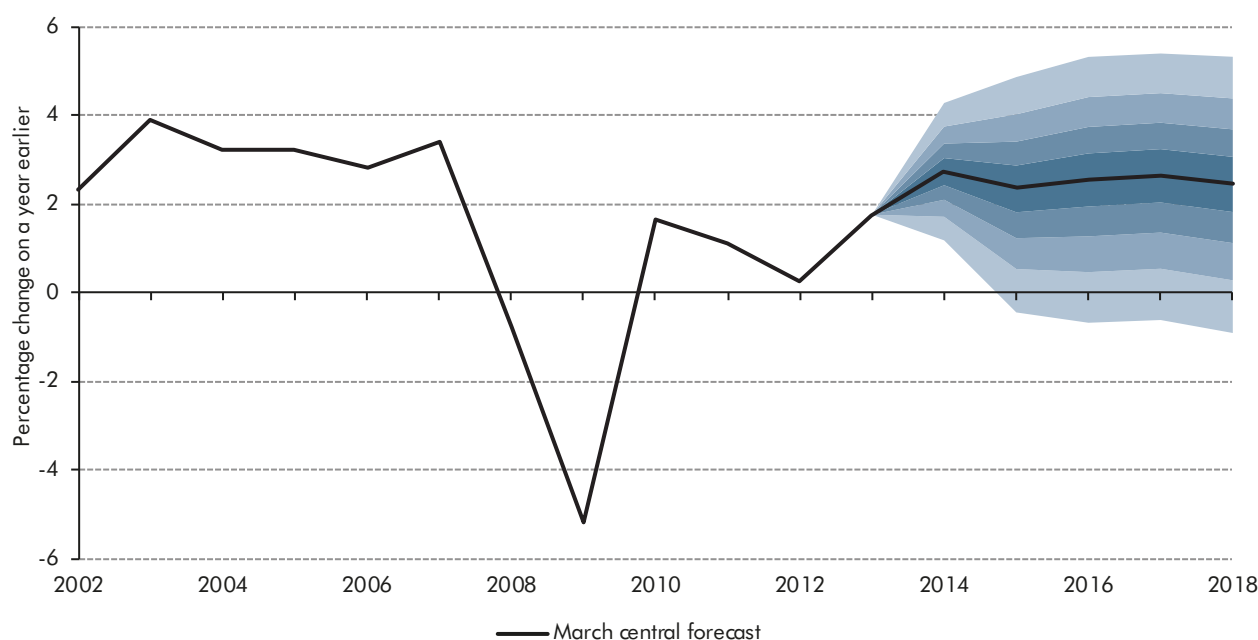
	Percentage change on a year earlier, unless otherwise stated						
	Outturn		Forecast				
	2012	2013	2014	2015	2016	2017	2018
Output at constant market prices							
Gross domestic product (GDP)	0.3	1.8	2.7	2.3	2.6	2.6	2.5
GDP levels (2012=100)	100.0	101.8	104.5	107.0	109.7	112.6	115.4
Output gap	-2.8	-2.2	-1.4	-1.1	-0.7	-0.3	0.0
Expenditure components of GDP							
Household consumption	1.5	2.3	2.1	1.8	2.5	2.7	2.4
General government consumption	1.6	0.9	1.2	-0.5	-1.2	-1.8	-0.9
Business investment	3.9	-1.2	8.0	9.2	8.1	8.7	7.7
General government investment	0.6	-6.4	10.7	1.0	2.2	0.8	-0.5
Net trade ¹	-0.7	0.1	-0.2	0.1	0.0	0.0	-0.1
Inflation							
CPI	2.8	2.6	1.9	2.0	2.0	2.0	2.0
Labour market							
Employment (millions)	29.5	29.9	30.4	30.6	30.9	31.2	31.4
Average earnings	2.0	1.5	2.5	3.2	3.6	3.7	3.8
LFS unemployment (% rate)	7.9	7.6	6.8	6.5	6.1	5.7	5.4
Claimant count (millions)	1.59	1.42	1.20	1.13	1.06	0.98	0.94
Changes since December forecast							
Output at constant market prices							
Gross domestic product (GDP)	0.1	0.3	0.3	0.1	0.0	0.0	-0.3
GDP levels (2012=100)	0.0	0.3	0.7	0.8	0.8	0.7	0.5
Output gap	-0.2	0.1	0.4	0.5	0.5	0.4	0.2
Expenditure components of GDP							
Household consumption	0.3	0.4	0.2	0.2	0.1	-0.2	-0.4
General government consumption	-0.1	0.3	0.8	0.1	-0.3	0.0	0.3
Business investment	1.2	4.2	2.9	0.6	-0.7	-0.2	-0.3
General government investment	-4.0	0.5	3.3	-0.1	0.1	0.3	0.6
Net trade	0.0	0.3	-0.2	0.0	0.0	0.0	0.0
Inflation							
CPI	0.0	0.0	-0.4	-0.1	0.0	0.0	0.0
Labour market							
Employment (millions)	0.0	0.0	0.2	0.2	0.2	0.2	0.2
Average earnings	0.0	0.1	0.0	-0.1	0.1	0.0	0.1
LFS unemployment (% rate)	0.0	0.0	-0.3	-0.4	-0.4	-0.4	-0.2
Claimant count (millions)	0.00	-0.01	-0.07	-0.10	-0.12	-0.15	-0.16

¹ Contribution to GDP growth.

1.24 We have revised up our employment forecast, with total employment expected to reach 31.4 million or 59.9 per cent of the adult population in 2018. Unemployment is forecast to fall steadily over the coming years, reaching 7 per cent in the coming months, 6 per cent by the end of 2016 and settling at our estimate of its sustainable rate, around 5¼ per cent, in 2018. The path of unemployment is lower than we forecast in December.

- 1.25** Total market sector employment is forecast to rise by 3.3 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 1.0 million fall in general government employment.
- 1.26** We expect CPI inflation to remain close to the 2 per cent target through the forecast period. Relative to our December forecast, the extra downward pressure on inflation from a slightly stronger exchange rate broadly offsets the reduced downward pressure from there being less spare capacity in the economy.
- 1.27** We have revised our house price inflation forecast up again, reflecting greater momentum in house prices in recent months. We expect annual house price inflation to peak at more than 9 per cent later this year.
- 1.28** 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 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.

Chart 1.2: Real GDP growth fan chart



Source: ONS, OBR

The fiscal outlook

- 1.29** 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.

1.30 Underlying PSNB is expected to halve from its 11.0 per cent of GDP peak in 2009-10 to 5.5 per cent of GDP by 2014-15. The rate of decline slowed in recent years as the recovery faltered, but appears to have gathered pace again. Table 1.2 shows that we expect the deficit to continue falling over the next five years, reaching a small surplus in 2018-19.

1.31 As set out above, we consider the unexpected strength of GDP growth over the past year to have been largely cyclical. As such, downward revisions to borrowing across the forecast are largely cyclical, with little change on average to our estimates of the structural position of the public finances – cyclically-adjusted PSNB – over the forecast period.

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
Excluding Royal Mail and APF transfers							
Public sector net borrowing	7.3	6.6	5.5	4.2	2.4	0.8	-0.2
Cyclically-adjusted net borrowing	5.3	5.0	4.5	3.4	1.9	0.6	-0.3
Surplus on current budget	-5.9	-5.1	-3.9	-2.7	-0.9	0.5	1.5
Headline fiscal aggregates							
Public sector net borrowing	5.1	5.8	4.9	3.8	2.2	0.9	-0.1
Cyclically-adjusted net borrowing	3.1	4.3	3.8	3.0	1.7	0.7	-0.1
Surplus on current budget	-5.4	-4.4	-3.3	-2.3	-0.7	0.5	1.5
Fiscal mandate and supplementary target							
Cyclically-adjusted surplus on current budget	-3.5	-2.8	-2.2	-1.5	-0.2	0.7	1.5
Public sector net debt	74.2	74.5	77.3	78.7	78.3	76.5	74.2
Changes since December forecast							
Excluding Royal Mail and APF transfers							
Public sector net borrowing	0.0	-0.2	-0.1	-0.2	-0.4	-0.4	-0.1
Cyclically-adjusted net borrowing	-0.1	-0.2	0.2	0.1	0.0	-0.1	0.0
Surplus on current budget	0.1	0.2	0.1	0.2	0.3	0.3	0.1
Headline fiscal aggregates							
Public sector net borrowing	0.0	-0.2	0.0	-0.2	-0.4	-0.4	-0.1
Cyclically-adjusted net borrowing	-0.1	-0.2	0.2	0.1	0.0	-0.1	0.0
Surplus on current budget	0.1	0.2	0.0	0.2	0.3	0.3	0.1
Fiscal mandate and supplementary target							
Cyclically-adjusted surplus on current budget	0.2	0.1	-0.2	-0.2	0.0	0.0	0.0
Public sector net debt	0.3	-1.0	-1.0	-1.2	-1.6	-1.9	-1.8

1.32 Table 1.3 shows that we have reduced our forecasts for the underlying deficit in 2013-14 by £3.4 billion, thanks primarily to an upward revision to stamp duty receipts (due to higher house prices and property transactions) and a downward revision to debt interest costs (due to lower inflation). But borrowing in 2014-15 is little changed from our December forecast, in part because we expect social security spending to be higher and because stronger

growth in the UK is expected to raise EU contributions in that year (an effect we expect to unwind in the future due to the UK rebate).

- 1.33 We have revised borrowing lower in each subsequent year of the forecast, reflecting stronger receipts in every year and slightly lower spending from 2015-16. The downward revision averages almost £6 billion a year from 2015-16 to 2017-18, before falling to £2.6 billion in 2018-19. The improvement is smaller in 2018-19 because of slower GDP and employment growth once the output gap has closed, and the Government's assumption that it will raise total public spending in line with whole economy inflation in that year, the forecast for which we have revised higher since December. In 2018-19, we forecast the public finances to move into surplus for the first time in 18 years.

Table 1.3: Changes to underlying public sector net borrowing since December

	£ billion					
	Forecast					
	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Public sector net borrowing¹						
December forecast	111.2	96.0	78.7	51.1	23.4	-2.2
March forecast	107.8	95.5	75.2	44.5	16.5	-4.8
Change	-3.4	-0.6	-3.5	-6.6	-6.9	-2.6
<i>of which:</i>						
Changes in the receipts forecast ^{1,2}	-1.1	-2.0	-3.5	-4.7	-4.0	-2.5
Changes in the spending forecast ^{1,2}	-2.3	0.9	-0.6	-1.7	-2.2	0.3
Receipts measures in the Treasury's policy decision table	0.0	0.0	0.6	1.8	1.4	1.7
Spending measures in the Treasury's policy decision table	0.0	0.5	-0.1	-2.0	-2.1	-2.1

¹ Excluding APF transfers.

² This includes the re-allocation of the policy measure for tax free childcare announced in Budget 2013. More information is available in our online supplementary fiscal tables.

- 1.34 Our forecast suggests that underlying net borrowing will have fallen by 11.2 per cent of GDP over the nine years from 2009-10 (around £190 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, the contributions to this would be:

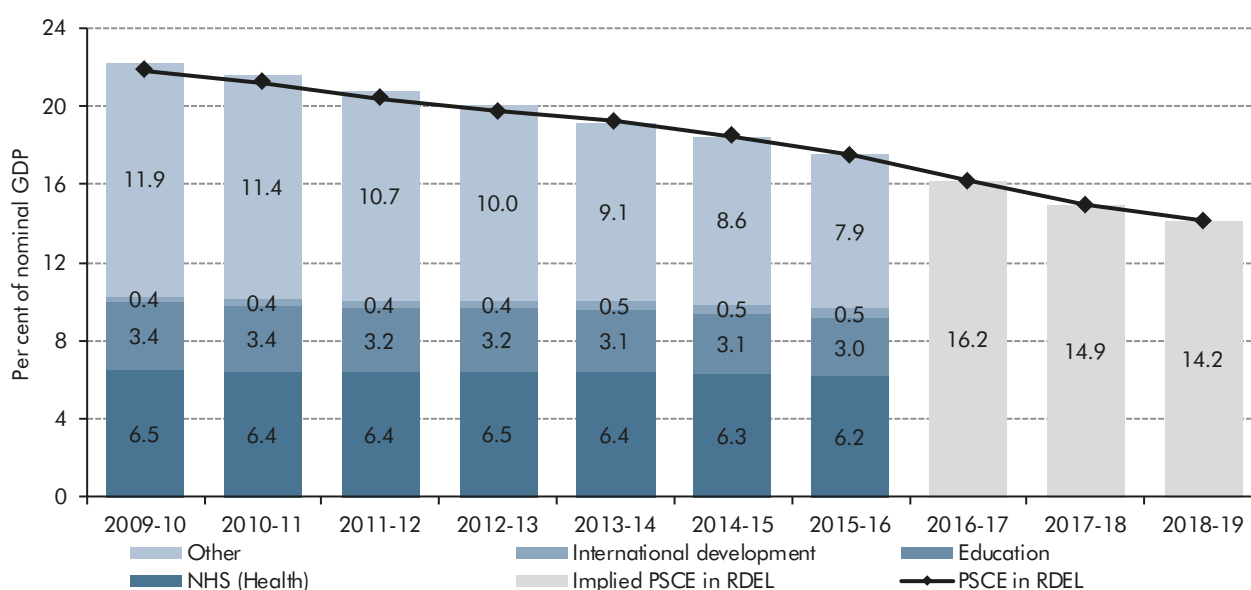
- 9.2 per cent of GDP, just over 80 per cent of the deficit reduction, from lower expenditure, with Total Managed Expenditure falling from 47.0 per cent of GDP in 2009-10 to 37.8 per cent of GDP by 2018-19. Within this total:¹
- PSCE in RDEL, a proxy for day-to-day spending on public services and administration, falls by 7.7 per cent of GDP, from 21.8 per cent of GDP in 2009-10 to 14.2 per cent in 2018-19, as shown in Chart 1.3. This is mirrored in our GDP forecast, where government consumption of goods and services falls from

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

23.2 per cent of nominal GDP in 2009 to 16.1 per cent by the end of the forecast, its lowest at least since 1948;

- PSGI in CDEL, public sector gross investment, falls by 1.6 per cent of GDP, from 3.5 per cent in 2009-10 to 1.9 per cent in 2018-19. In 2007-08, PSGI in CDEL was 2.7 per cent of GDP; and
- social security spending falls by 1.1 per cent of GDP, from 11.1 per cent in 2009-10 to 10.0 per cent in 2018-19, approaching its pre-crisis level.
- 2.0 per cent of GDP, just under 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, and strong growth in capital taxes like stamp duty and inheritance tax.

Chart 1.3: Current spending on public services and administration



Plans for RDEL excluding depreciation upto 2015-16. Beyond 2015-16 based on implied PSCE in RDEL calculated from the Government assumption for TME. Other includes unallocated amounts.

Source: HM Treasury Budget 2014, HM Treasury Public Expenditure Statistical Analyses, July 2013

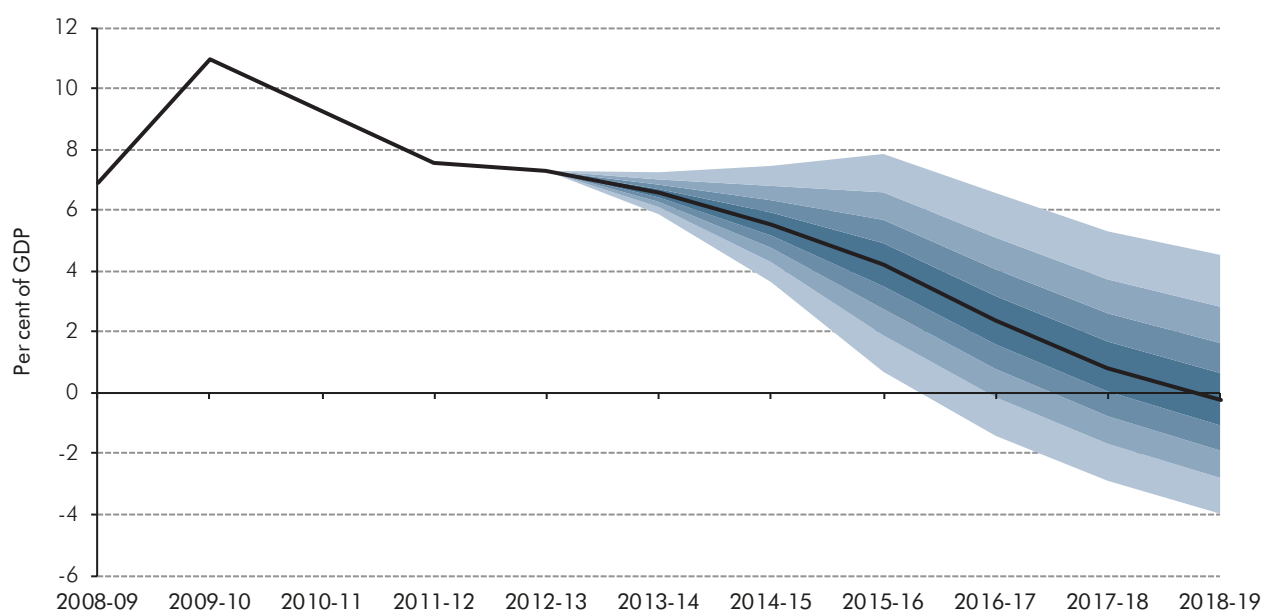
1.35 The current budget balance, which excludes borrowing to finance net investment spending, is forecast to show a deficit of £71.5 billion this year (£83.7 billion on an underlying basis), down from a peak of £108.9 billion in 2009-10. The current balance moves into surplus in 2017-18 and records a surplus of £30.5 billion in 2018-19. With planned investment spending little changed, revisions to the current balance are similar to those to PSNB.

1.36 The cyclically-adjusted current budget (CACB) moves from a deficit of 2.8 per cent of GDP in 2013-14 to a surplus of 1.5 per cent of GDP in 2018-19. We expect the CACB to move

into surplus in 2017-18. As with cyclically-adjusted PSNB, the CACB is little changed on average over the forecast period.

- 1.37 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 past official forecast errors were 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.

- 1.38 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 78.7 per cent of GDP. It then falls by a small margin in 2016-17 and more rapidly thereafter, reaching 74.2 per cent of GDP in 2018-19. PSND in 2018-19 is forecast to be 1.8 per cent of GDP lower than we forecast in December. Table 1.4 breaks this change down as follows:
- upward revisions to our nominal GDP forecast have reduced the ratio of the cash value of debt to GDP in each year, with the effect rising from 0.4 per cent of GDP in 2013-14 to 0.6 per cent of GDP in 2018-19; and
 - our forecast for PSND in cash terms is lower by £10 billion in 2013-14, rising to £25 billion in 2018-19. In the near term, the largest effect is from the cash flow measure of borrowing this year being revised down by more than the headline measure. In later years, cumulative revisions to net borrowing are more important.

Table 1.4: Changes to public sector net debt since December

	Per cent of GDP						
	Outturn	Forecast					
		2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
December forecast	73.9	75.5	78.3	80.0	79.9	78.4	75.9
March forecast	74.2	74.5	77.3	78.7	78.3	76.5	74.2
Change	0.3	-1.0	-1.0	-1.2	-1.6	-1.9	-1.8
<i>of which:</i>							
Change in nominal GDP ¹	0.1	-0.4	-0.5	-0.5	-0.6	-0.7	-0.6
Change in cash level of net debt	0.2	-0.6	-0.6	-0.7	-0.9	-1.2	-1.2
£ billion							
December forecast	1182	1269	1365	1451	1515	1554	1573
March forecast	1185	1258	1355	1439	1497	1530	1548
Change in cash level of net debt	3	-10	-10	-13	-18	-24	-25
<i>of which:</i>							
Budget measures	0	0	1	2	4	6	8
Other changes in net borrowing	0	-4	-4	-8	-14	-21	-23
Other	3	-7	-6	-6	-8	-9	-9

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

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

1.39 Later this year, the ONS will implement significant revisions to the public finance statistics. For this *EFO*, our forecasts are presented on the existing basis, but we have provided a preliminary assessment of the possible implications of future revisions in Annex B. These methodological and classification changes are expected to raise the measured level of net debt by around £140 billion in 2014-15, falling to around £125 billion by 2018-19. This is equivalent to around 7¾ and 6 per cent of our current forecasts for nominal GDP respectively. But at the same time the ONS is also expected to revise nominal GDP higher, by roughly 2½ to 5 per cent. A revision in middle of this range would reduce the upward revision to the debt to GDP ratio to around 4¾ per cent of GDP in 2013-14 and around 3¼ per cent in 2018-19. It is important to stress that these are changes to the way the public sector's finances are measured, not to the underlying activities being measured.

Performance against the fiscal targets

1.40 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.

1.41 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 1.5 per cent of GDP in 2018-19, fractionally less than we forecast in December.

- 1.42 PSND is forecast to rise to a peak of 78.7 per cent of GDP in 2015-16, which is slightly lower than we forecast in December. However, as in each of our *EFOs* since December 2012, our forecast does not show the Government on course to achieve the supplementary target – we forecast that debt will rise by 1.5 per cent of GDP in the target year, down from an increase of 1.7 per cent of GDP in our December forecast.
- 1.43 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 75 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, implying a positive output gap in the target year, the structural position of the public finances would be worse. 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 65 per cent. The level of potential output would need to be over 2 per cent lower in 2018-19 than in our central forecast to make it more likely than not that the mandate would be missed; and
 - third, by looking at alternative economic scenarios. We have looked at two scenarios where interest rates are higher than assumed in our central forecast. In one scenario, that happens for good reasons – stronger growth in household incomes and company profits. In the other scenario, it happens for bad reasons – instability in emerging markets intensifies, triggering risk aversion that drives up credit spreads meaning interest rates facing households and companies rise without corresponding increases in incomes and profits. The Government would continue to meet the fiscal mandate in both scenarios, reflecting the substantial CACB surplus in 2018-19 in our central forecast. The supplementary debt target would be missed in the bad scenario, but met by a very small margin in the good scenario.
- 1.44 The forthcoming ONS revisions to the public finances data are unlikely to have a significant impact on the measured CACB at the forecast horizon, and thus on the Government's chances of meeting the fiscal mandate. But even though the measured level of net debt will be significantly higher after the revisions, the chances of it falling in 2015-16 are likely to be greater if the APF starts selling gilts before the end of 2015-16, as assumed in our central forecast – although still not greater than 50 per cent. Debt would also fall more steeply if the Government was to sell more of the shares that it purchased as a result of financial interventions. This does not feature in our central forecast, given uncertainties over the potential scale and timing of such sales.