



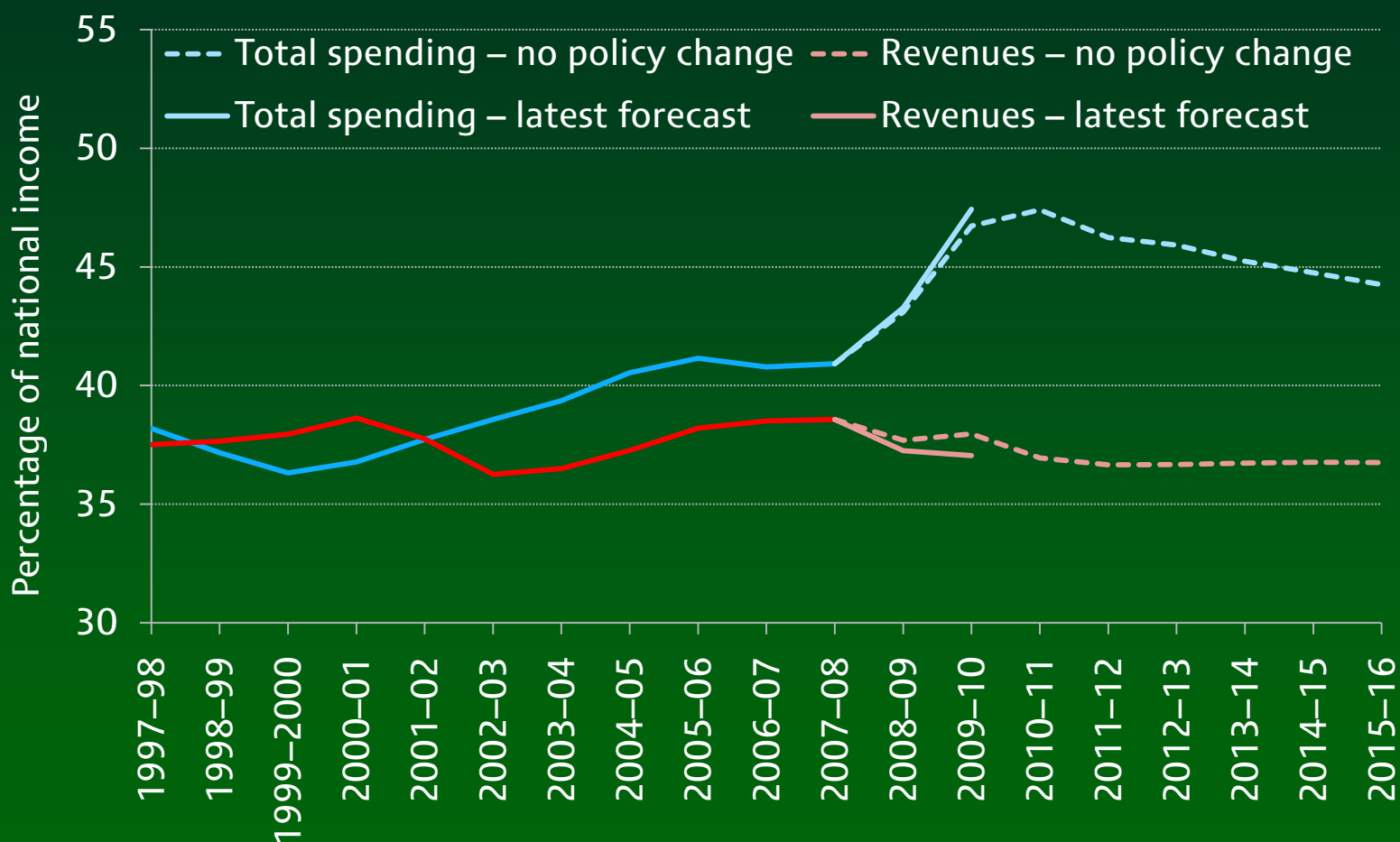
Institute for
Fiscal Studies



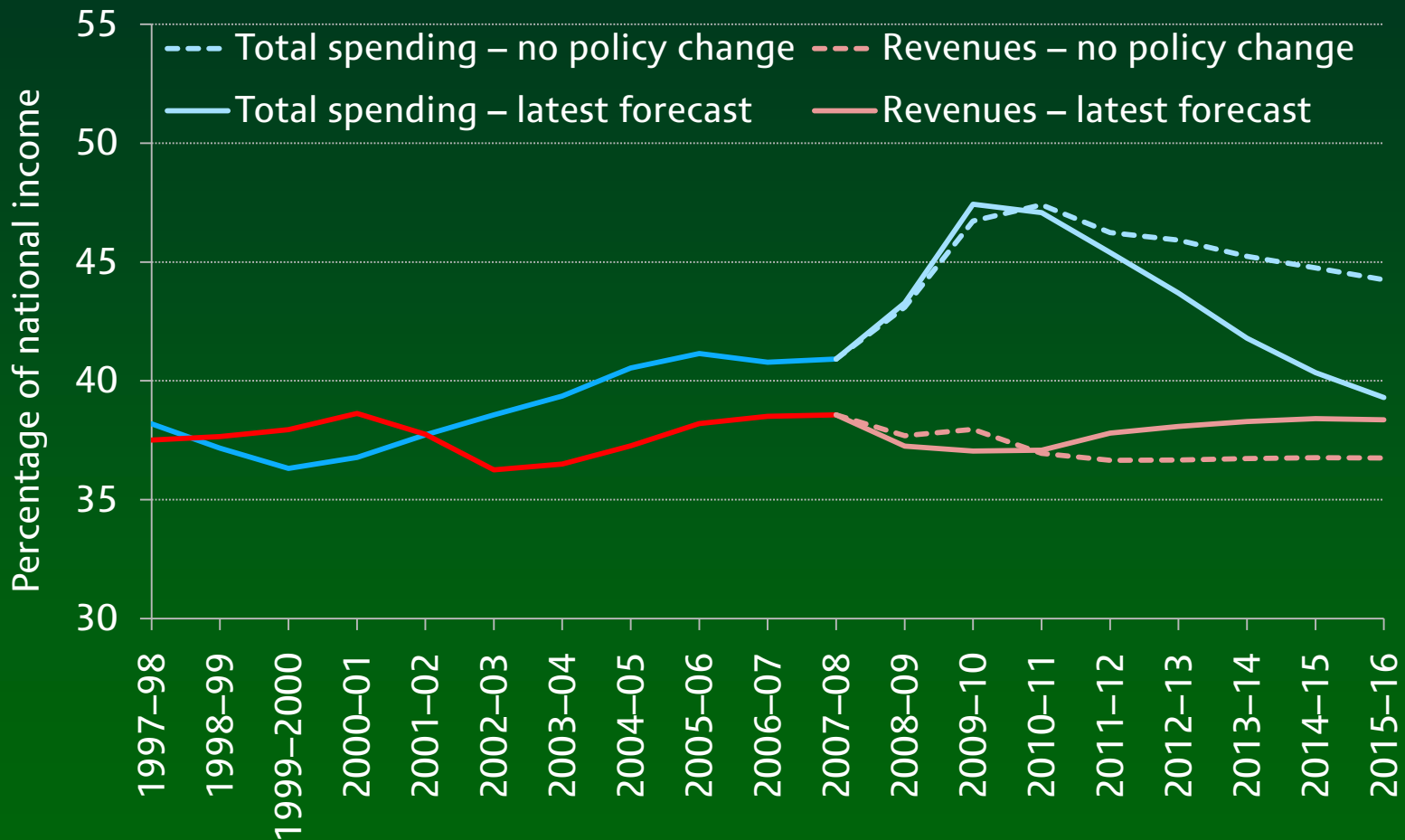
The new fiscal framework: an assessment

Rowena Crawford, Carl Emmerson and Gemma Tetlow

The story so far



The story so far



The new fiscal framework

- Two new fiscal targets:
 - The fiscal mandate
 - The supplementary target
- Set up independent Office for Budget Responsibility (OBR)
 - Prepare economic and fiscal forecasts
 - Assess the extent to which the fiscal mandate has been, or is likely to be achieved
 - Analyse the sustainability of the public finances
 - Assess the accuracy of its previous fiscal and economic forecasts

The fiscal mandate (1/2)

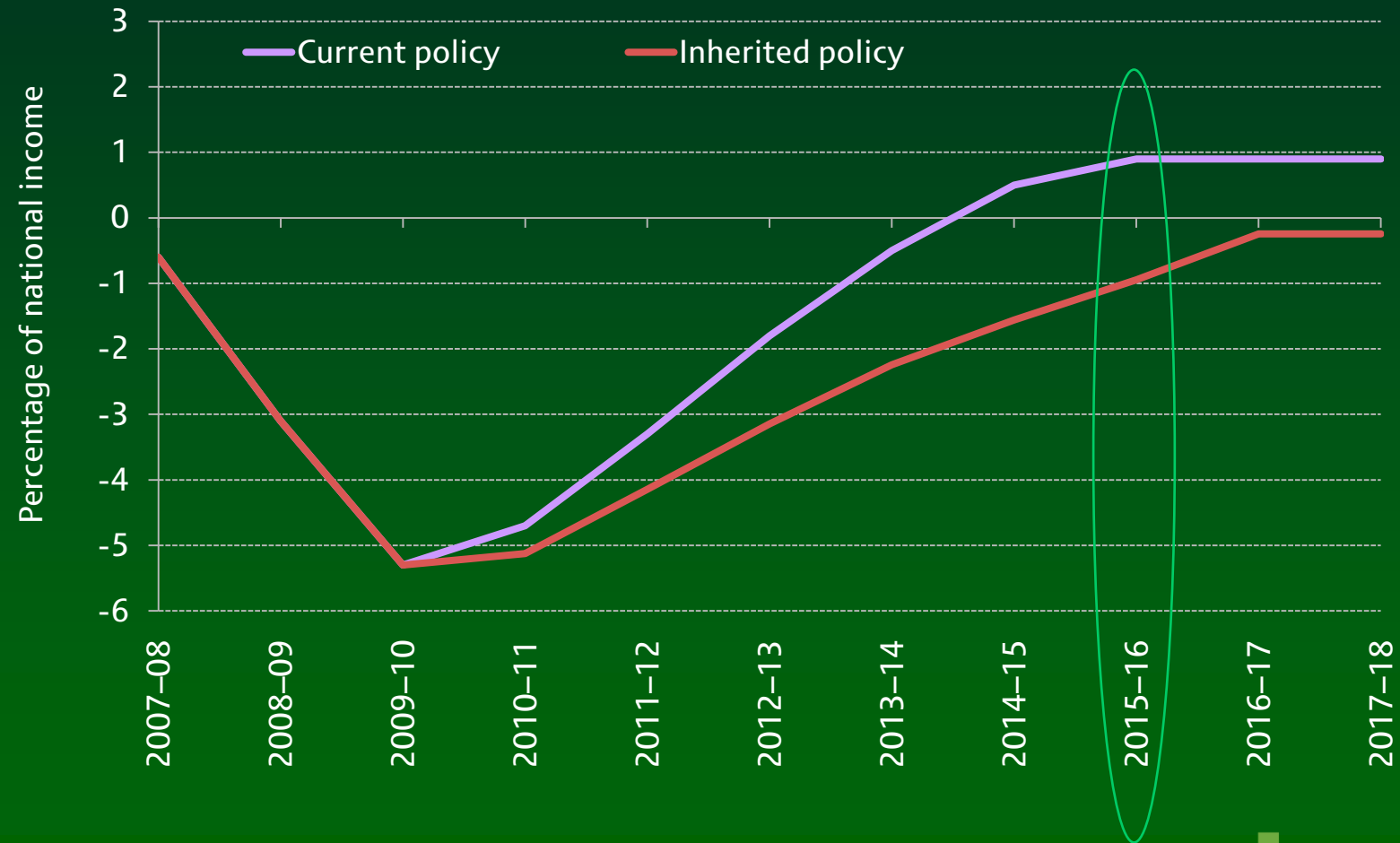
- “To achieve cyclically-adjusted current budget balance by the end of the rolling, five-year forecast horizon”
- Essentially a new ‘golden rule’
 - Appropriate for governments to borrow to finance investment spending but not day-to-day spending
 - Allows borrowing to be higher when the economy is thought to be temporarily weak
 - (Both desirable features)

The fiscal mandate (2/2)

- “To achieve cyclically-adjusted current budget balance by the end of the rolling, five-year forecast horizon”
- Difference in how the new fiscal mandate is operationalised
 - Forward-looking
 - Potential problems of interpretation
- A greater than 50% chance of meeting the mandate is equivalent to a forecast cyclically-adjusted current budget surplus

Will the fiscal mandate be 'met'?

Forecast cyclically-adjusted current budget under...

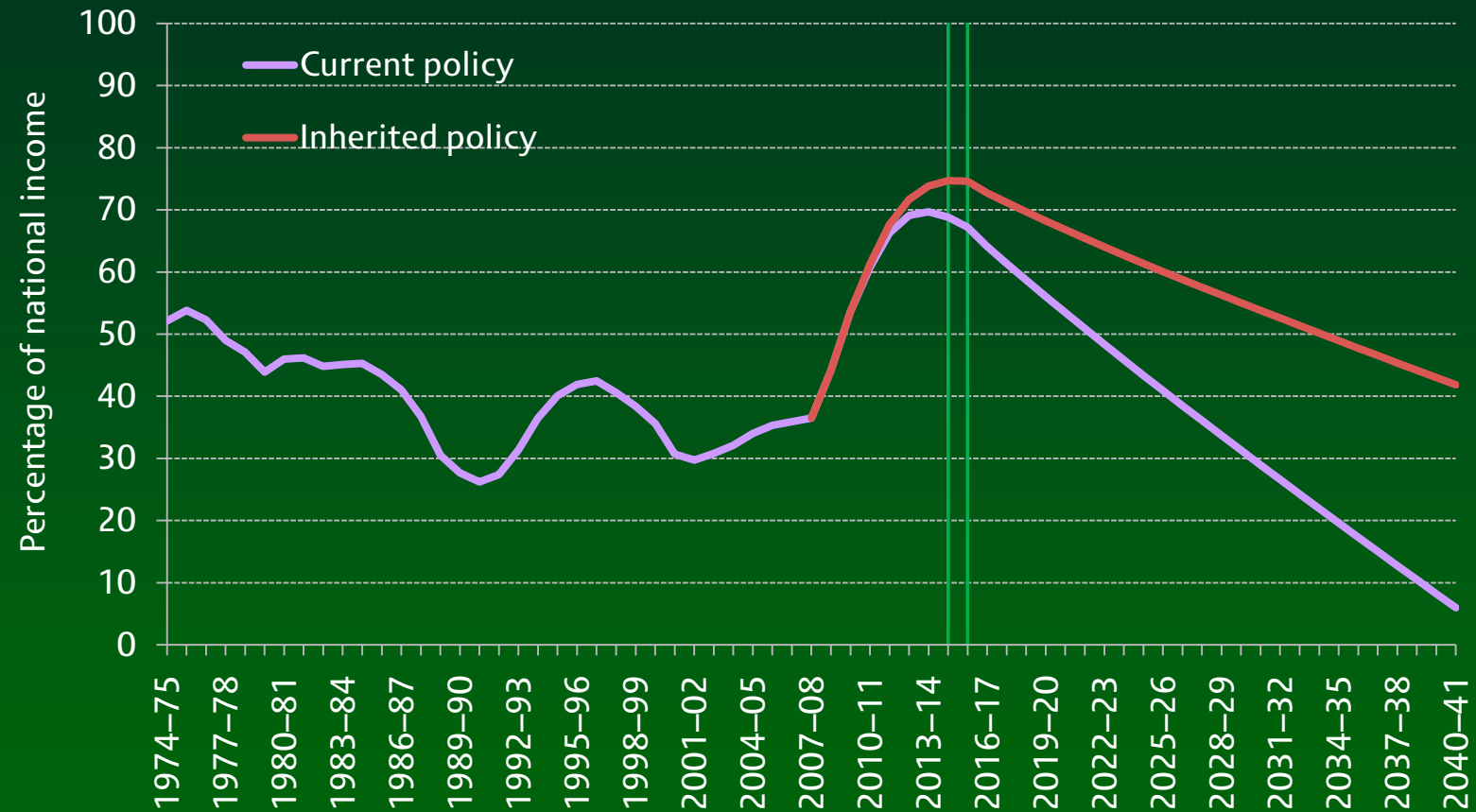


The supplementary target

- “public sector net debt as a percentage of national income to be falling at a fixed date of 2015-16”

Will the supplementary target be met?

Forecast public sector net debt under...



Will these targets ensure fiscal sustainability?

- No
- Fiscal mandate
 - Constrains forecasts not outturns
 - Needs careful monitoring to ensure forward looking nature not manipulated (existence of the OBR should help)
- Supplementary target
 - Is only binding in one year
 - Will become obsolete after 2015-16

Replacing the supplementary target

- The government intends to introduce a new target for debt as a share of national income
 - Based on an assessment by the OBR of the long-term sustainability of the public finances
- Issues to consider:
 - Long term pressures on the public finances: e.g. demographics
 - Consider a broader measure of indebtedness than public sector net debt: include other long term liabilities such as pension promises?
 - Perhaps target level of pre-committed annual payments rather than total level of indebtedness?

The Office for Budget Responsibility (1/2)

- Improved the presentation, transparency and credibility of official forecasts
- Welcome increases in transparency:
 - Explanation of the fiscal forecasting process
 - Publication of key economic assumptions underlying fiscal forecasts
 - Central forecasts (no unquantified degree of ‘caution’ built in)
- Further improvements in transparency possible
 - Particularly regarding their macroeconomic forecasts
 - How and why do forecasts differ from those of the Bank of England?

The Office for Budget Responsibility (2/2)

- Degree of interaction between the OBR and government
 - Interaction could damage the perception of the OBR as independent
 - + Interaction aids policy making
 - ⇒ Interaction should continue but need to be open about it
- Not allowed to consider alternative policy scenarios
 - + Avoids danger of being drawn into political discussion
 - Would inform public debate (especially prior to elections)
 - ⇒ Certainly want ‘no policy change’ forecasts published

Summary

- New fiscal mandate
 - Desirable in its forward looking nature
 - Will require careful monitoring to ensure not abused
 - OBR forecasts it will be met under current policies
- Supplementary target
 - OBR forecasts it will be met under current policies
 - Will need replacing
- Office for Budget Responsibility
 - Has improved the presentation, transparency and credibility of official forecasts
 - Should help ensure fiscal sustainability in future



Institute for
Fiscal Studies



The new fiscal framework: an assessment

Rowena Crawford, Carl Emmerson and Gemma Tetlow