Green Budget public finance forecasts

Robert Chote, Rowena Crawford, Carl Emmerson and Gemma Tetlow
Summary

• Green Budget baseline forecast
  – Current budget deficit and public sector net borrowing in 2009–10 to be £10.4 billion lower than PBR forecast
  – Over next five years: gap reduces as our forecast for growth in tax receipts lower than Treasury’s
  – Public sector net debt peaks at a lower level

• Barclays economic forecasts
  – Worse outlook for the macro economy
  – Implies borrowing remains at a higher level

• Budget judgement
  – Repair public finances more quickly, but not immediately
  – Additional £13 billion tightening by 2015–16
  – No significant additional tightening should be implemented in 2010–11
Forecasts for 2009–10

<table>
<thead>
<tr>
<th>£ billion</th>
<th>PBR December 2009</th>
<th>Green Budget February 2010</th>
<th>Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current receipts</td>
<td>498.1</td>
<td>505.2</td>
<td>+7.1</td>
</tr>
<tr>
<td>Current spending</td>
<td>626.2</td>
<td>623.0</td>
<td>−3.2</td>
</tr>
<tr>
<td>Current budget surplus</td>
<td>−128.1</td>
<td>−117.7</td>
<td>+10.4</td>
</tr>
<tr>
<td>Net investment</td>
<td>49.5</td>
<td>49.5</td>
<td>0.0</td>
</tr>
<tr>
<td>Borrowing</td>
<td>177.6</td>
<td>167.2</td>
<td>−10.4</td>
</tr>
</tbody>
</table>
2009–10: Explaining the difference

- Receipts (+£7.1 billion)
  - Income tax (+£3.3 billion)
  - National Insurance contributions (+£1.1 billion)
  - VAT (+£2.8 billion)
2009–10: Explaining the difference

• Receipts (+£7.1 billion)
  – Income tax (+£3.3 billion)
    • Receipts have not fallen as quickly since November as PBR 2009 forecast
    • Adjusted for likely loss of income tax revenue from bank payroll tax
  – National Insurance contributions (+£1.1 billion)
  – VAT (+£2.8 billion)
2009–10: Explaining the difference

• Receipts (+£7.1 billion)
  – Income tax (+£3.3 billion)
  – National Insurance contributions (+£1.1 billion)
    • Receipts have actually risen since November, compared to PBR 2009 forecast of a cash fall
    • Additional NICs revenue expected from bank payroll tax
  – VAT (+£2.8 billion)
2009–10: Explaining the difference

- Receipts (+£7.1 billion)
  - Income tax (+£3.3 billion)
  - National Insurance contributions (+£1.1 billion)
  - VAT (+£2.8 billion)

- Trends over year to date, adjusted for the change in the main rate from January, suggest total VAT revenues will exceed PBR forecast
2009–10: Explaining the difference

- Receipts (+£7.1 billion)
  - Income tax (+£3.3 billion)
  - National Insurance contributions (+£1.1 billion)
  - VAT (+£2.8 billion)

- Spending (–£3.2 billion):
  - Central government spending growing less quickly so far this year than PBR 2009 forecast
  - Extrapolating trend would suggest £8.7 billion under-spend
Medium-term forecasts: baseline assumptions

- Economy performs broadly as the Treasury expects
- Corporation tax
  - Barclays ‘optimistic’ case forecast for corporate profits growth in 2010–11 and 2011–12
  - Receipts grow thereafter to move back towards long-run average
Medium-term forecasts: receipts
Medium-term forecast: spending

• Current spending in 2010–11
  – Assume same non-debt interest spending, slightly lower debt interest spending

• Current spending from 2011–12
  – Assume same real growth as PBR

• Investment spending from 2010–11 onwards
  – Assume same proportion of GDP as PBR
Medium-term forecast: borrowing and debt

- **Current budget deficit**
  - 2009–10: £10.4 billion smaller
  - 2010–11: £7.2 billion smaller
  - Medium-term: falls to 2.9% in 2014–15, compared to 3.2% in PBR

- **Public sector net borrowing**
  - 2009–10: £167 billion
  - 2010–11: £169 billion
  - Medium-term: falls to 4.1% in 2014–15, compared to 4.4% in PBR

- **Public sector net debt**
  - Rises to 76.0% of GDP in 2014–15
  - Lower than PBR forecast of 77.7%
Uncertainties around the macroeconomic outlook

• Barclays macro forecasts suggest risks are on the downside
  – Larger permanent loss of potential output?
  – Permanently lower trend growth?

• Barclays alternative macro scenarios
  – Central: 7½% permanent loss of potential, 1¾% trend growth
  – ‘Optimistic’: 5% permanent loss, 2¼% trend growth
  – ‘Pessimistic’: 10% permanent loss, 1¾% trend growth

• Implications for the public finances
  – Forecast for borrowing this year and next very similar
  – But more of it likely to be structural
  – More policy action needed to meet Government’s fiscal targets
Public sector net borrowing: alternative forecasts

Percentage of national income

- PBR 2009
- Green Budget: baseline
- Green Budget: Barclays 'optimistic'
- Green Budget: Barclays central
- Green Budget: Barclays 'pessimistic'

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Public sector net debt: alternative forecasts

- PBR 2009
- Green Budget: baseline
- Green Budget: Barclays 'optimistic'
- Green Budget: Barclays central
- Green Budget: Barclays 'pessimistic'

Percentage of national income

Years: 08-09, 09-10, 10-11, 11-12, 12-13, 13-14, 14-15

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Conclusions

• Key challenge: repair public finances credibly and sustainably without damaging economic recovery
  – Current plans rely on general public and markets believing a fiscal consolidation plan that lasts for two parliaments

• Budget judgement
  – Increase planned tightening over the next parliament to 5.0% of GDP (or an extra £13 billion) by 2015–16: doing more of required consolidation sooner would aid credibility and add room for manoeuvre if things turn out worse than PBR expects
  – But no further tightening should be implemented in 2010–11: large tightening already in place and monetary policy likely to remain loose

• Things are almost certain to turn out different from PBR forecasts: Government should be clear about how their plans will adapt

• Additional independent scrutiny of forecasts would aid credibility
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