Budget 2016: a takeaway Budget to keep on course to meet budget surplus target?

Carl Emmerson and Paul Johnson

Presentation to BBC journalists, 7 & 8 March 2016
Eliminating the deficit?

Source: http://budgetresponsibility.org.uk/data/
Achieving and maintaining a budget surplus would be a break from the past

Notes and sources: see Figure 3.1 of The IFS Green Budget: February 2016.
Borrowing in 2015–16

- OBR November 2015 forecast is for borrowing of £73.5bn
  - compares to £74.1bn forecast in July 2015

- Extrapolating borrowing over the first ten months of this financial year implies borrowing of just under £80 billion

- But £4 billion of the apparent overshoot is from rapid growth in investment spending which might not persist

- Borrowing of around £76 billion would be above, but very close to, the OBR’s forecast
Budget: Small downwards revision to growth?

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- Bank, and independent forecasters have slightly downgraded their forecasts since November
- None of these forecasts stand if Brexit occurs
Inflation forecasts also down

- Chancellor likely to highlight that lower inflation reduces forecast debt interest spending

- But overall lower inflation bad for the public finances
  - freezing most working age benefits and 1% cap on public sector pay would deliver smaller real saving
  - fixed cash spending plans for public services more generous in real terms
  - in cash terms saving from lower debt interest spending more-than-offset by lower VAT revenues

- One response would be to trim departmental spending limits
  - could reduce cash limits and leave planned real spending cut unchanged
Medium-term risks: revenues

• Earnings 1% lower costs £5 billion
  – Bank of England’s latest forecast has earnings more than 1% lower than their November forecast

• FTSE All-Share 7% lower than assumed by OBR’s autumn forecast
  – £2 billion hit to capital tax revenues unless the stock market recovers

• Oil prices falls directly depress revenues from North Sea oil and gas production
  – OBR estimates slightly more than offset by increased revenues elsewhere
  – but low oil price places pressure on Chancellor to reduce North Sea taxes
Medium-term risks: spending

- Cuts this parliament significantly less than expected
  - And less than last parliament
- But
  - Spending falling to historically low levels
  - Public sector pay due to fall to lowest level relative to private sector for decades
  - Additional demographic and cost pressures
Planned cuts to spending

2010–11 to 2019–20:
Total spending: −1.8% (£13.8bn)
Debt interest: +6.7% (£2.9bn)
Non-debt interest: −2.3% (£16.8bn)
Planned cuts to spending

2010–11 to 2019–20:
- Non-debt interest: -2.3% (£16.8bn)
- Social security: -1.1% (£2.3bn)
- Public services: -2.8% (£14.4bn)

Non-debt interest spending
Public service spending
Social security + TCs

Total social security: -1.1% (£2.3bn)
GB pensioner benefits: +10.0% (£10.6bn)
Non-pensioner benefits: -13.1% (£12.9bn)
Planned cuts to spending

2010–11 to 2019–20:
- Non-debt interest: –2.3% (‒£16.8bn)
- Social security: –1.1% (‒£2.3bn)
- Public services: –2.8% (‒£14.4bn)

Central government departmental spending: –12.4% (‒£49.6bn)
‘Unprotected’ central government spending (not NHS, Education, DfID or Defence): –25.8% (‒£45.7bn)
Measures already in the pipeline (1/2)
(April 2016 unless otherwise stated)

• Benefit cuts including freeze to most working age benefits until April 2020
• 1% cut to social rents each year for four years
• 1% ceiling on public sector pay awards for four years
• Above inflation increases in personal allowance and higher rate threshold
  – to £10,800–£11,000 and £42,700–£43,000
• National Living Wage introduced at £7.20/hr (vs £6.70 min wage for <25s)
• Increases in company car tax
• Increases in tobacco duties
• Employment Allowance increased to £3,000
• Corporation tax rate cut to 19% in April 2017 and 18% in April 2020
  – annual investment allowance increased to be £200k
• Apprenticeship levy introduced at 0.5% of wage bill above £3 million
• Bank levy to be cut each January through to 2021
• Various temporary business rate reliefs expire during 2016
Measures already in the pipeline (2/2)
(April 2016 unless otherwise stated)

• New personal savings allowance of £1,000 for basic rate taxpayers and £500 for higher rate taxpayers
  – cash ISAs to move to a net rather than gross annual contribution limit
• New £5,000 dividend tax allowance introduced, dividend tax rates up
• Pensions lifetime allowance cut to £1m; annual allowance tapered away from £40k at £150k to £10k at £210k
• Contracting out for DB schemes ended
• Single tier pension introduced
• Inheritance tax threshold frozen until April 2021, new main residence allowance introduced at £100k in April 2017 rising to £175k in April 2020
• Increased rate of stamp duty on purchases of non-main residential property
• Mortgage interest relief for non-corporate landlords restricted to basic rate from April 2017
New policies?

• Promise to raise tax free personal allowance to £12,500 and higher rate threshold to £50,000 by 2020
  – costs £8 billion
• Low prices offer a chance to raise fuel duties
  – 1p on petrol and diesel raises c £500m
• Restriction of interest deductibility for corporation tax is on the cards
• Further relief for North Sea oil?
• Pension tax changes now look unlikely
  – changes to lifetime and annual allowances possible
• Prime Minister has said that a “Help to save” scheme to encourage those on low incomes to save will be announced
• More “stealth taxes”?
Summary

• Good reasons to aim to reduce debt as a share of national income but commitment to deliver budget surpluses from 2019–20 risky

• Outlook for public finances weakened since the Autumn
  – lower inflation, weaker outlook for earnings growth, poor stock market performance all depress receipts

• Delivering planned cuts to public service spending won’t be easy

• Meeting commitment to cut income tax would come at considerable cost

• Net takeaways likely if £10bn forecast surplus in 2019–20 is to be retained
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