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Spring Statement 2019: modest windfall banked (for now)

Carl Emmerson

Borrowing forecast revised down again

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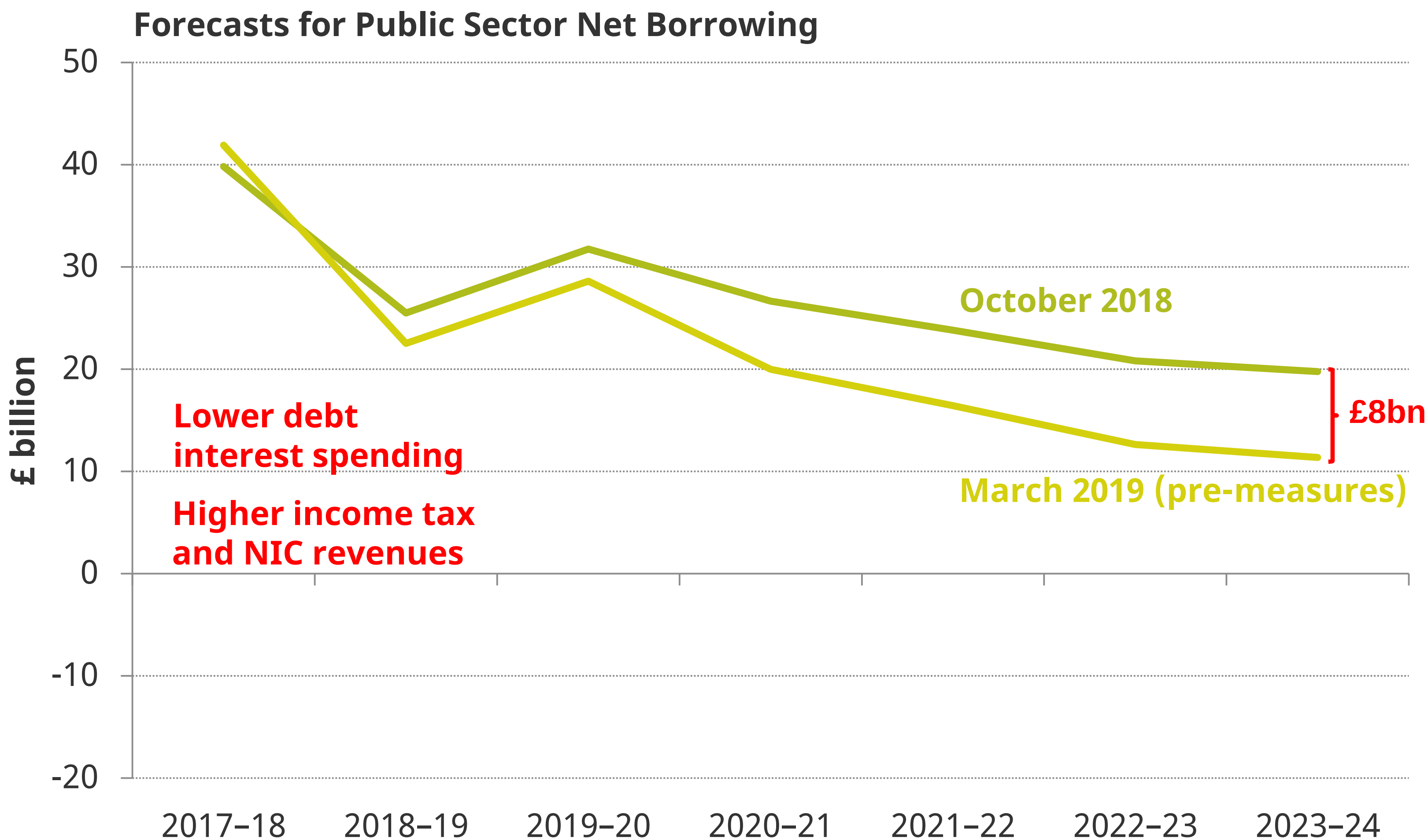
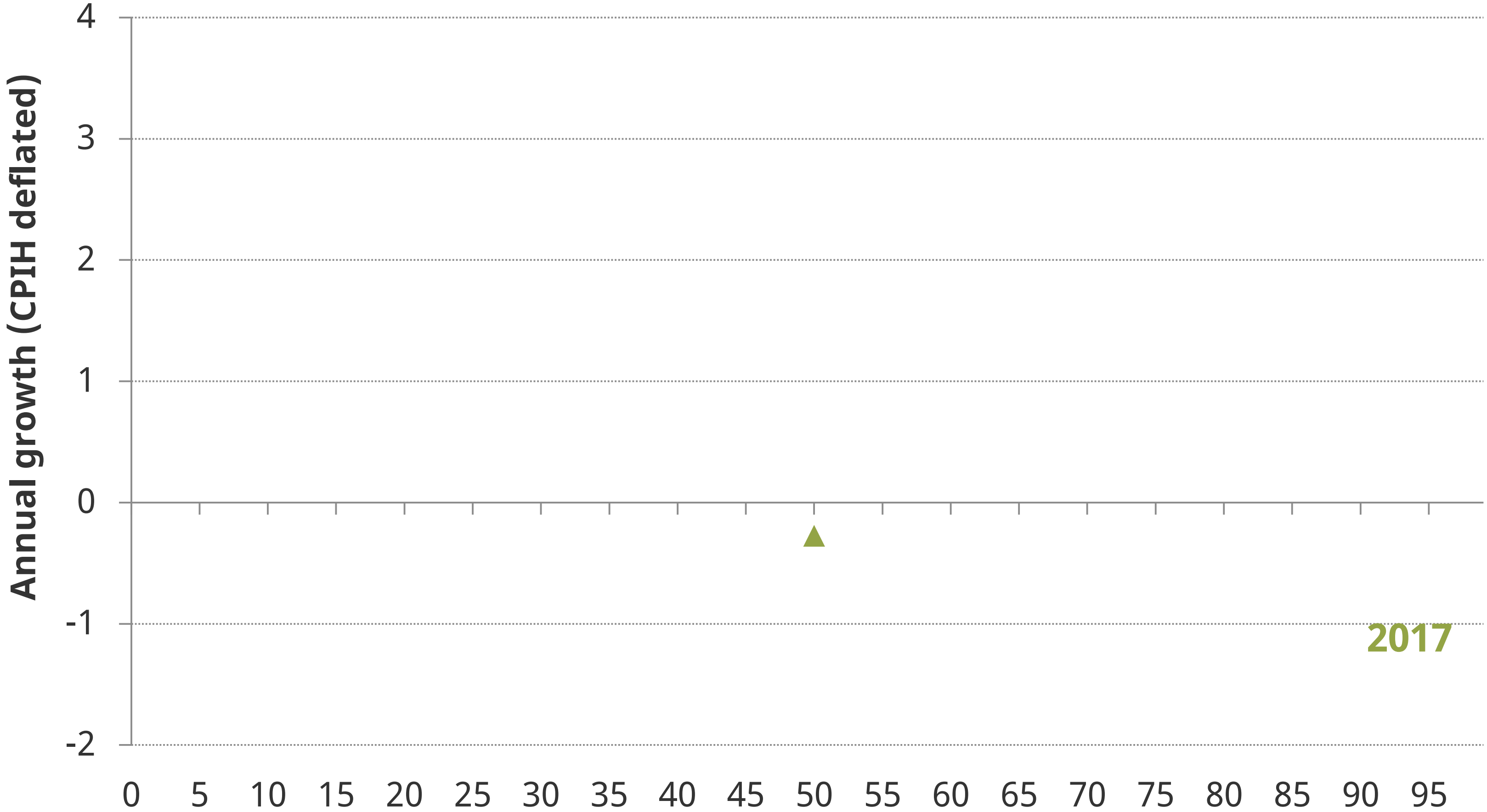


Source: Office for Budget Responsibility *Economic and Fiscal Outlook.*

Faster growth in earnings towards the top of the distribution, boosting revenues



Source: Author's calculations using data from the Annual Survey of Hours and Earnings.

Faster growth in earnings towards the top of the distribution, boosting revenues

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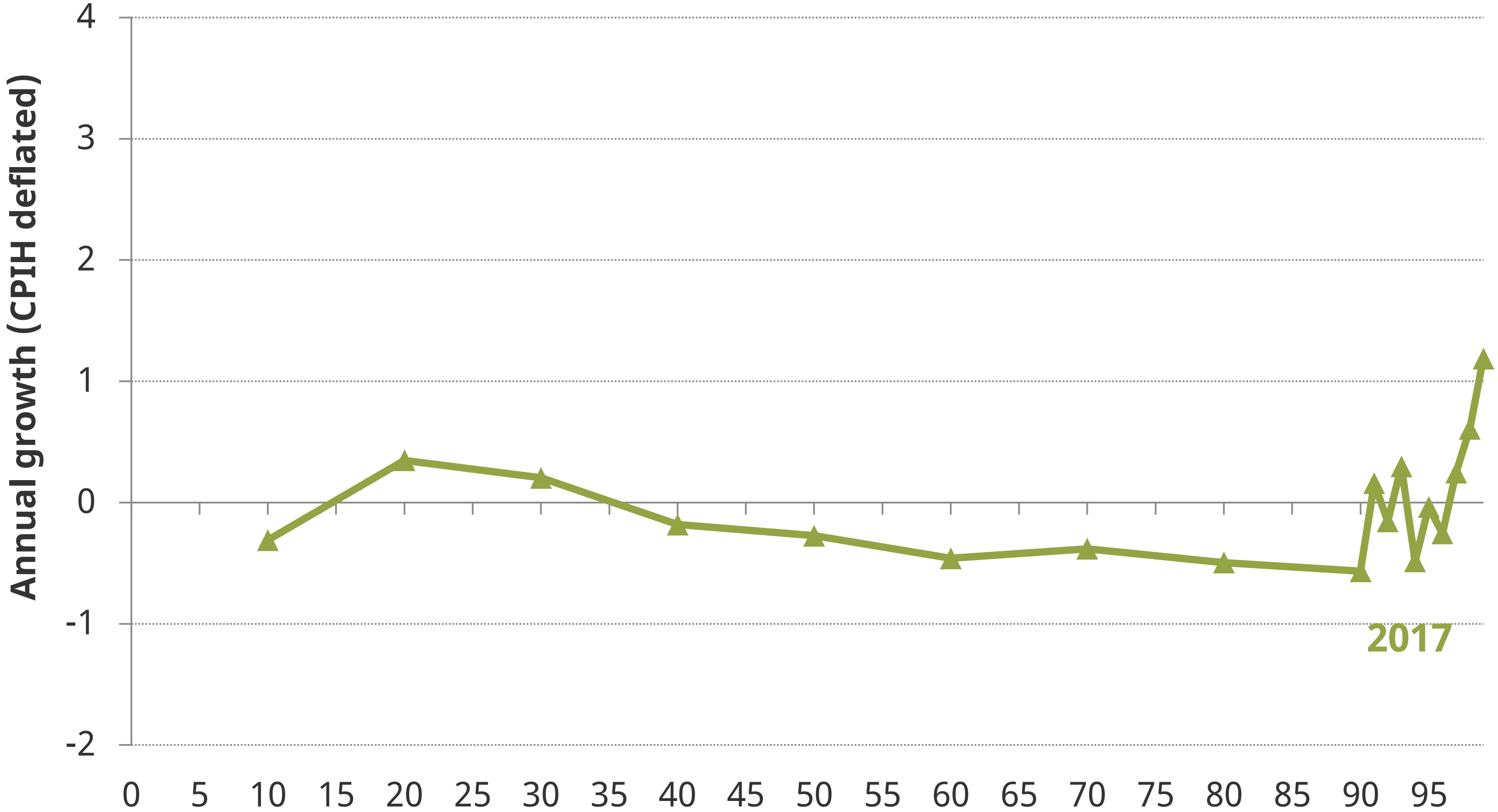

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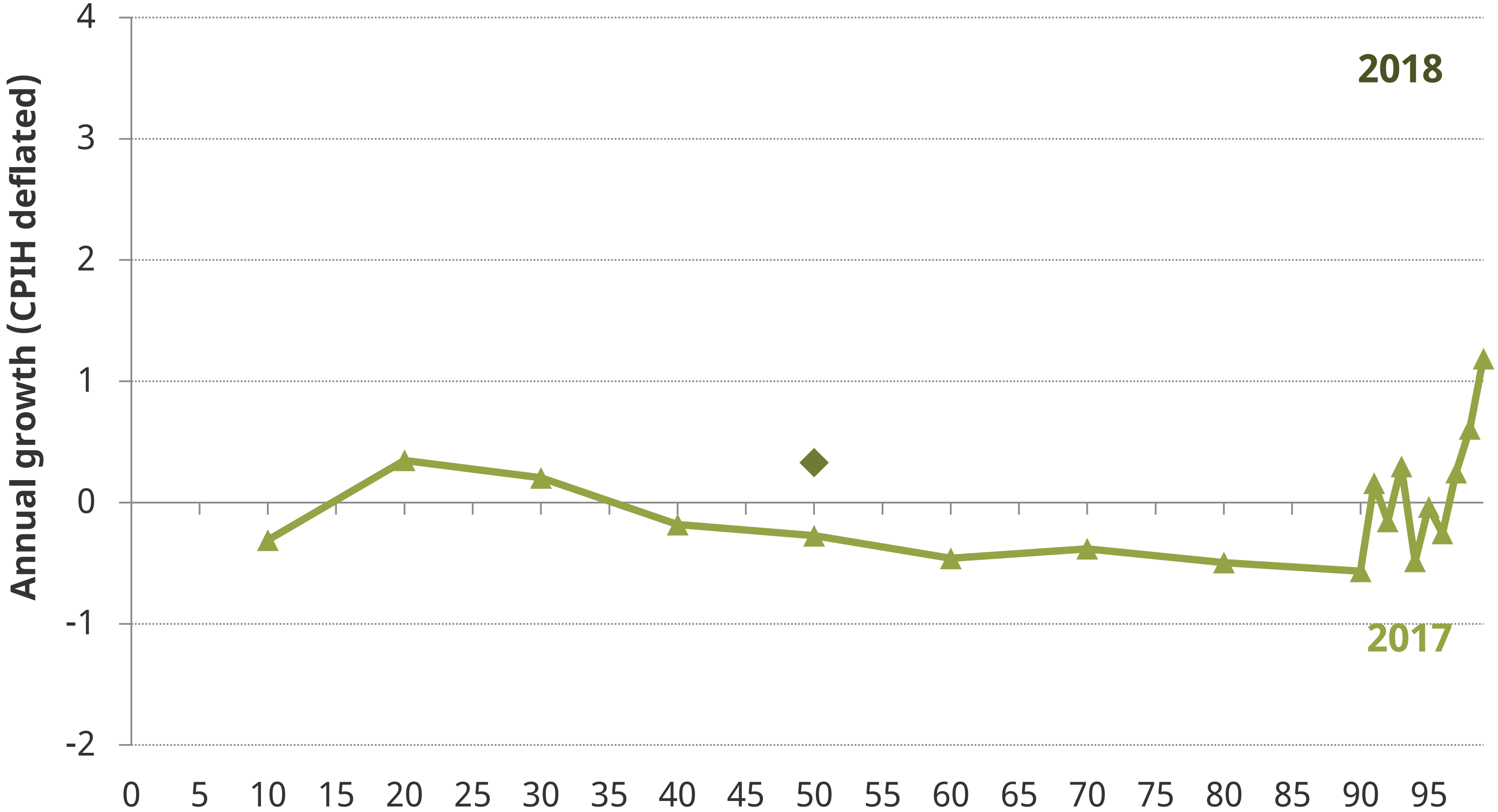

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Faster growth in earnings towards the top of the distribution, boosting revenues

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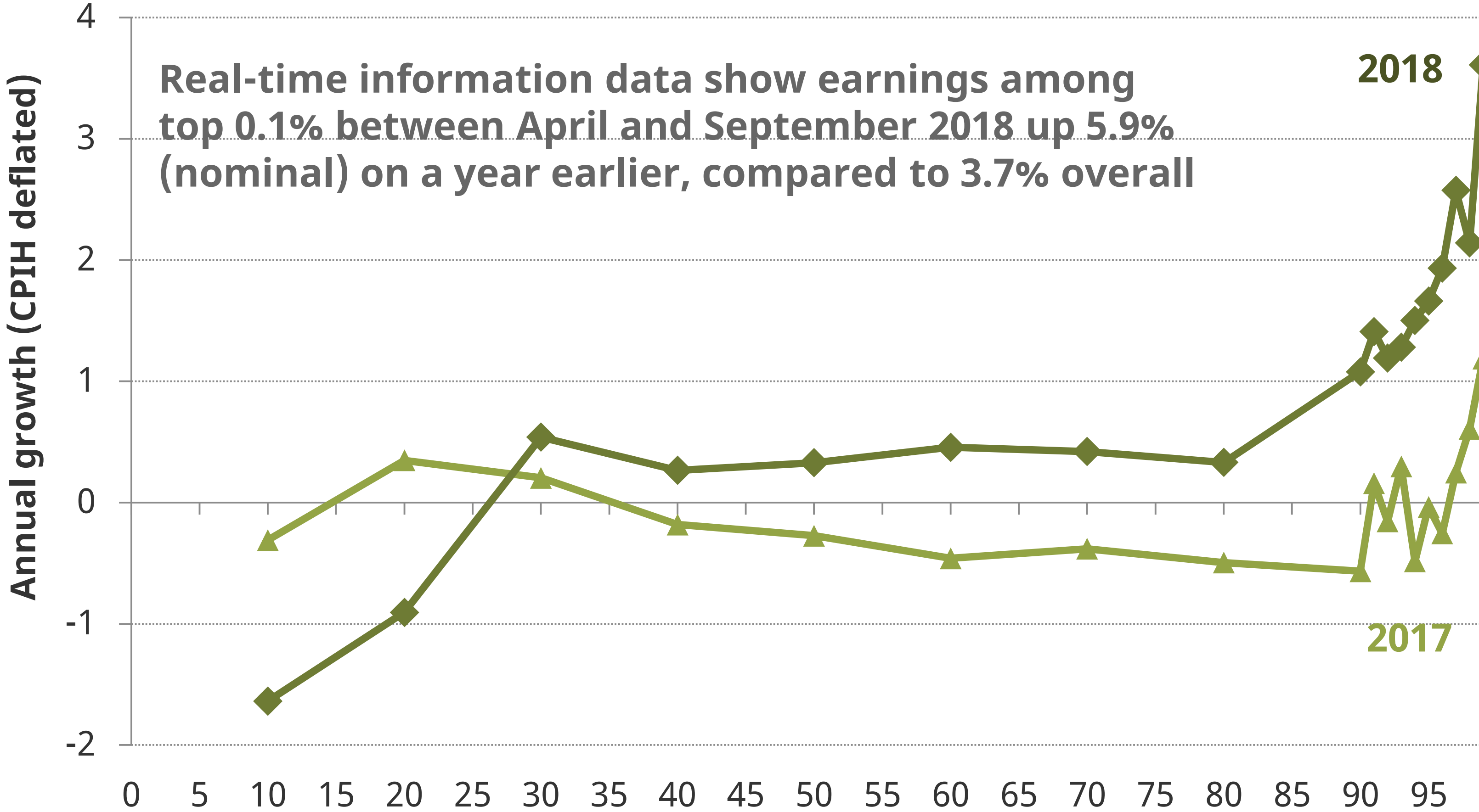

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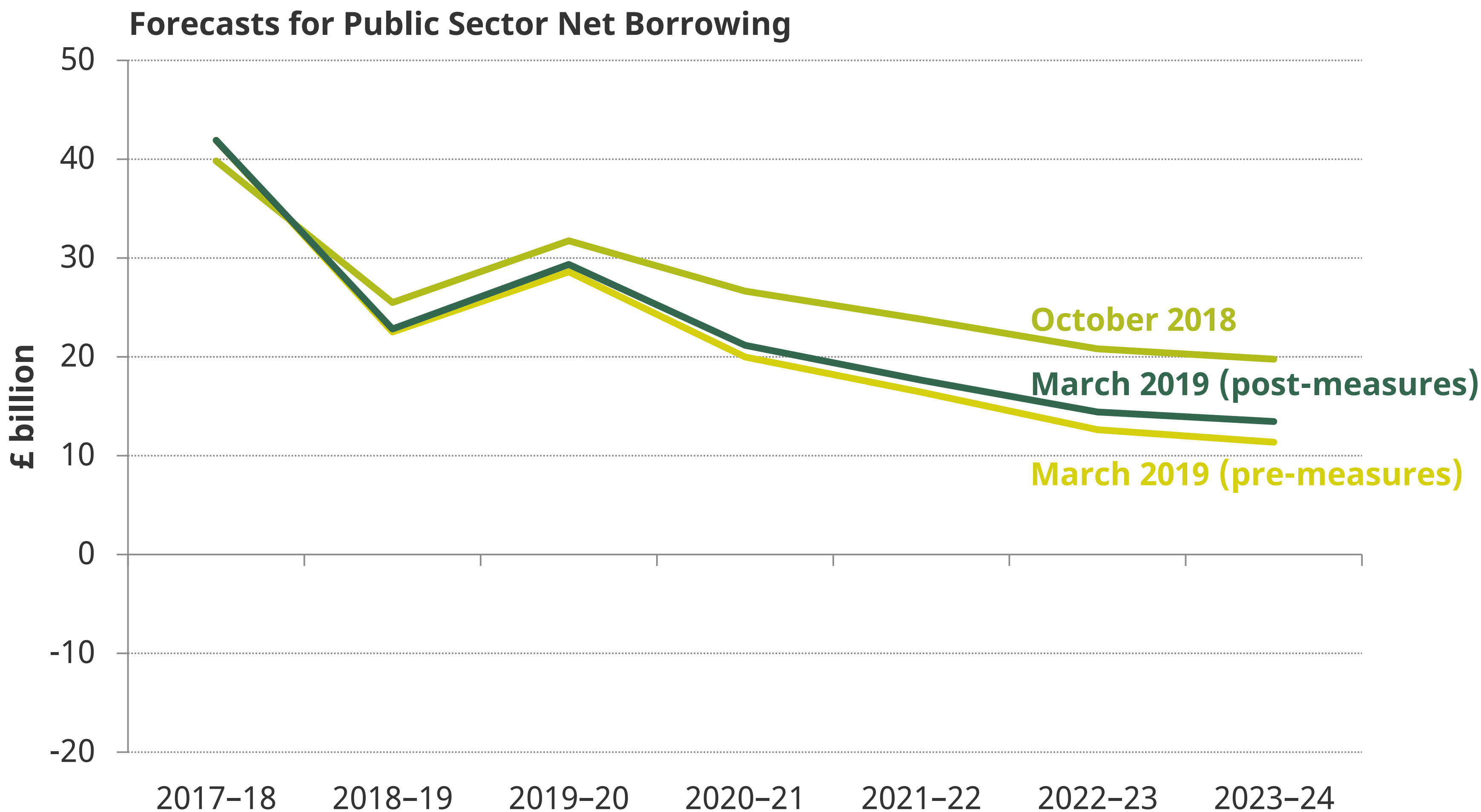
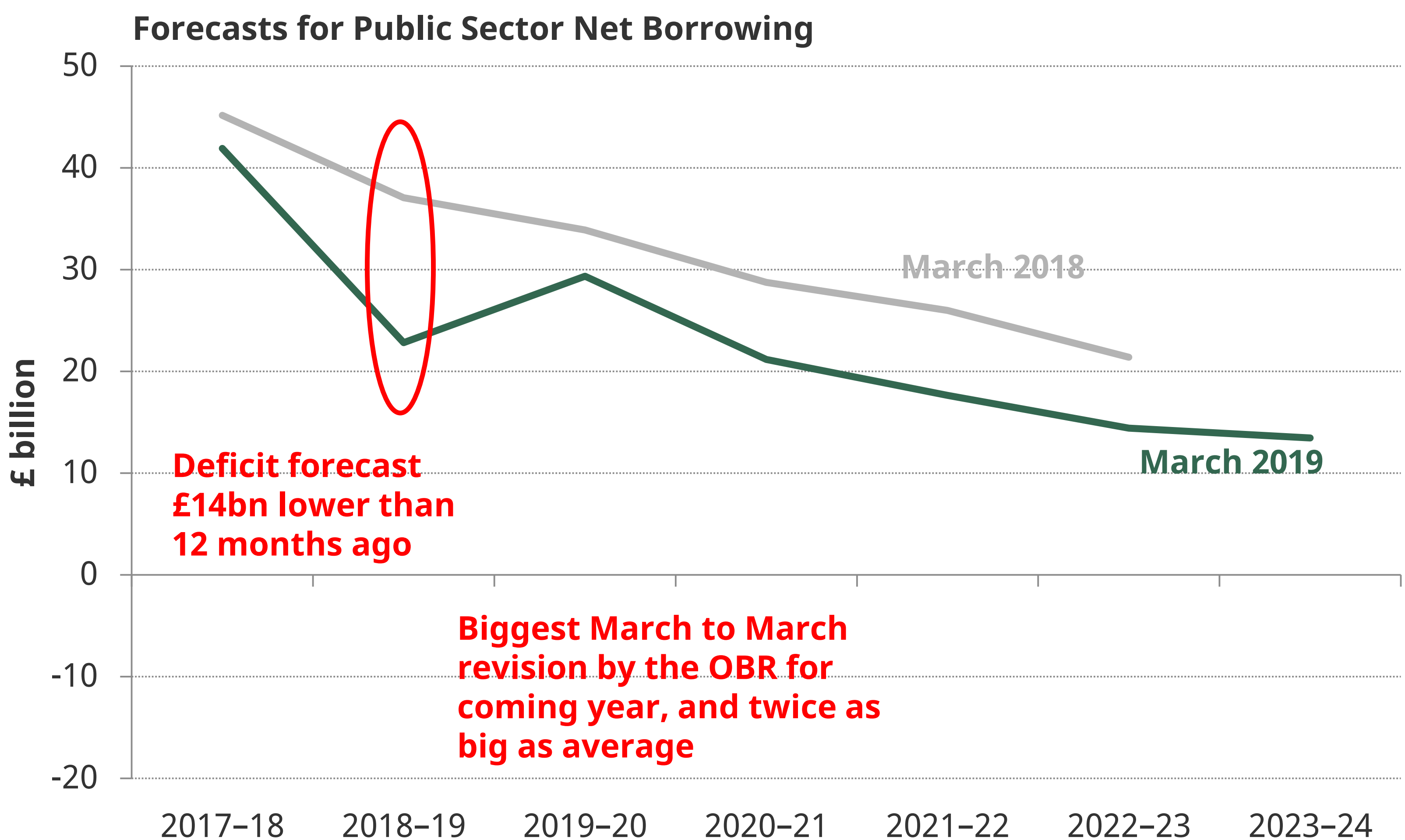
Chancellor chose to bank most of the windfall



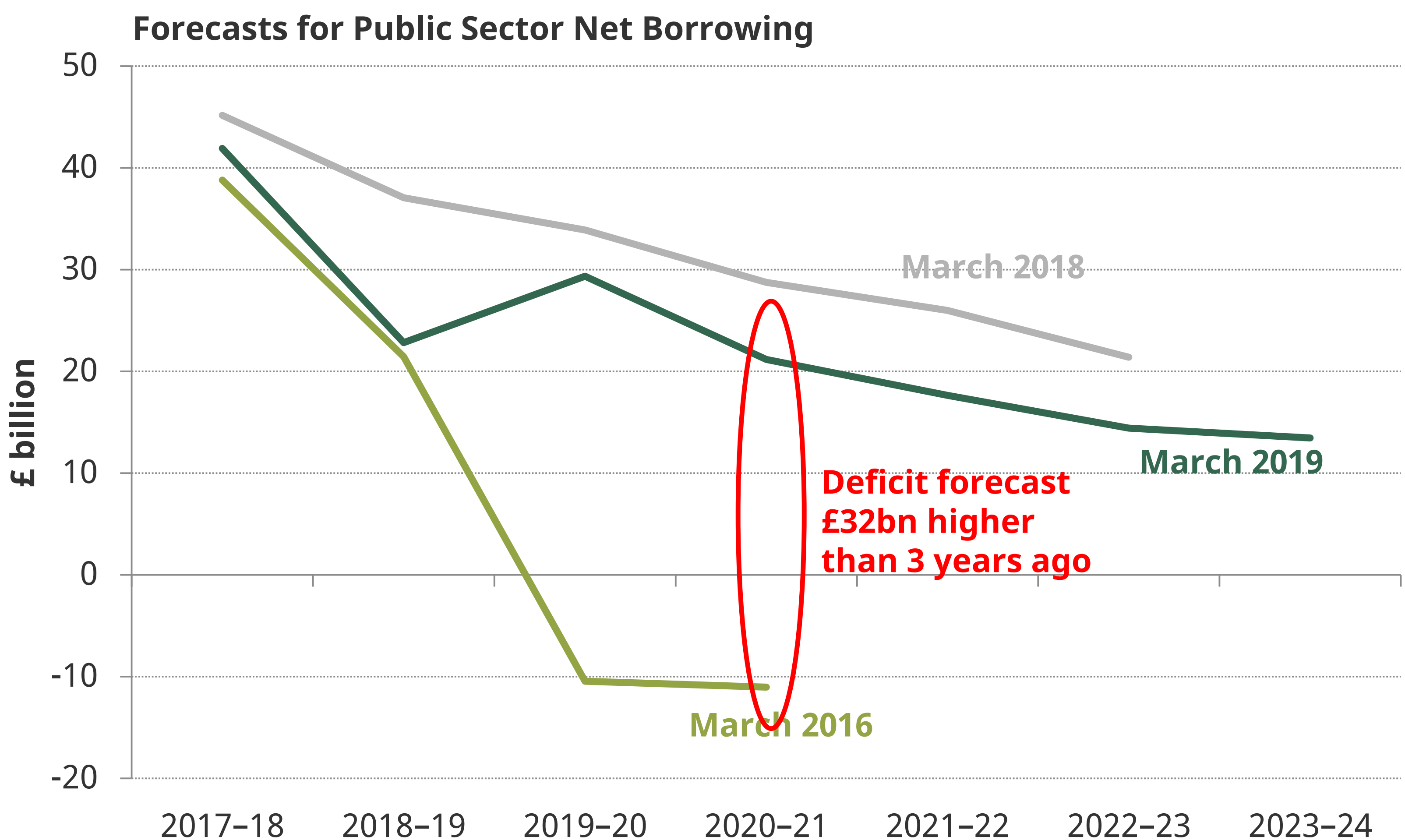
Source: Office for Budget Responsibility *Economic and Fiscal Outlook*

Deficit forecast much lower than a year ago



Source: Office for Budget Responsibility *Economic and Fiscal Outlook*

Deficit forecast much higher than 3 years ago



Source: Office for Budget Responsibility *Economic and Fiscal Outlook*

Fiscal targets (1/2)

Three targets set for current parliament

- cyclical borrowing below 2% of GDP in 2020–21

Currently on course to meet fiscal mandate with some room to spare

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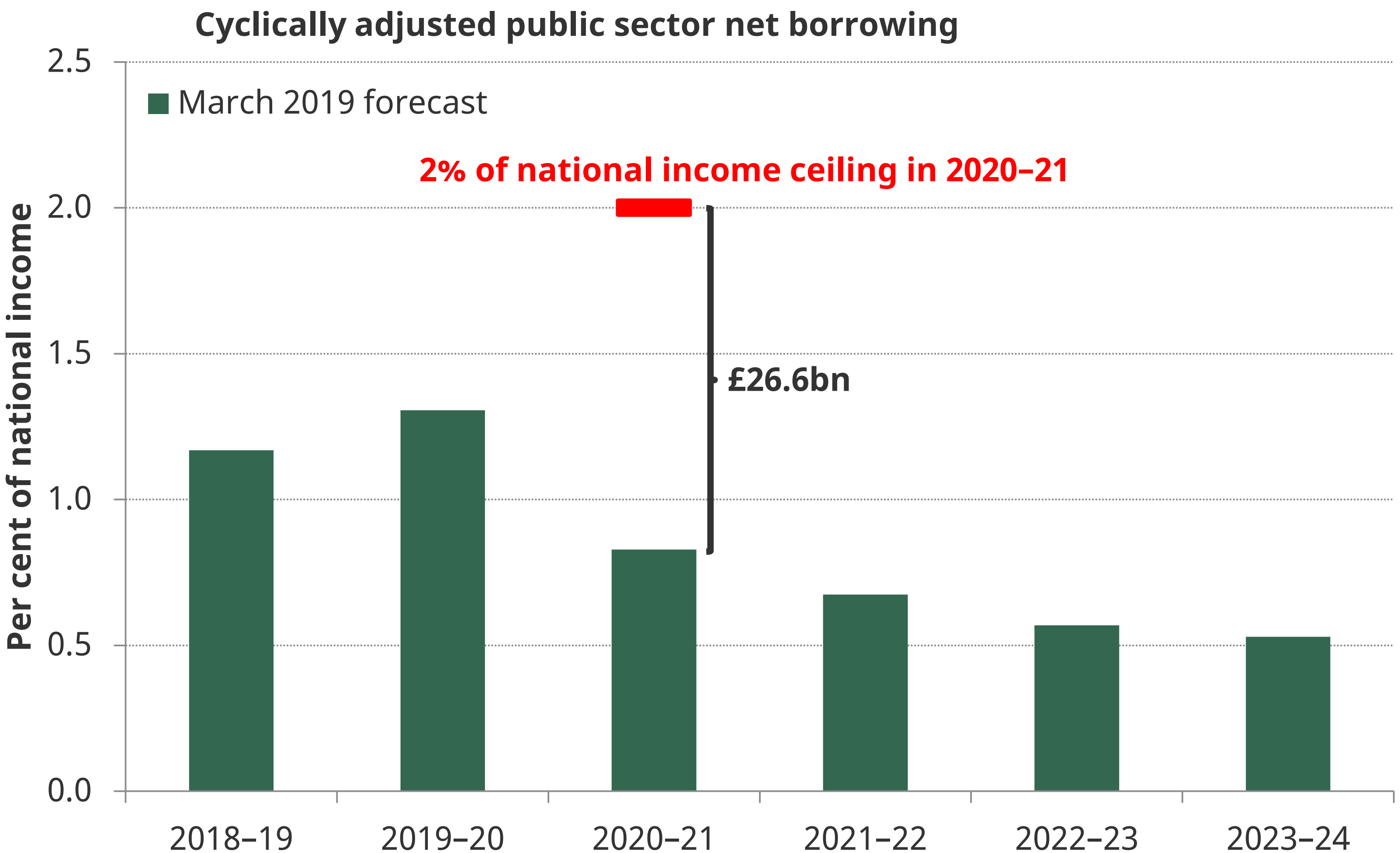

Source: Office for Budget Responsibility *Economic and Fiscal Outlook*

Improvement to student loan accounting will increase headline borrowing significantly

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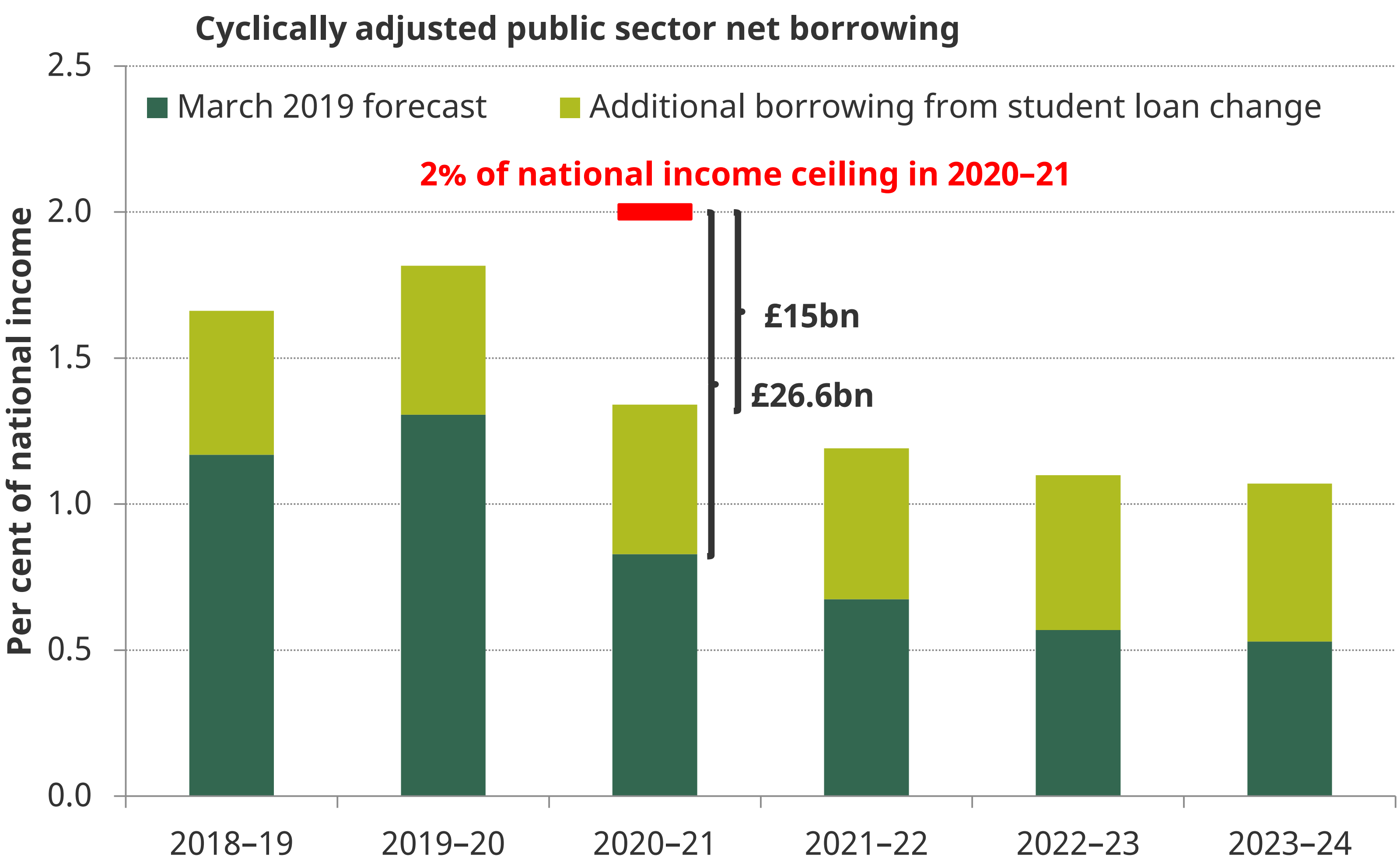


Source: Office for Budget Responsibility *Economic and Fiscal Outlook*

Fiscal targets (1/2)

Three targets set for current parliament

- cyclical borrowing below 2% of GDP in 2020–21
- debt to fall as a share of GDP in 2020–21
- welfare spending below cash cap in 2022–23

On course to meet all three

- but in two years time none can be breached in the current parliament

Chancellor did not mention goal of "a balanced budget by the middle of the next decade"

- not currently on course to meet this
- and far from clear that policy is being set with this in mind

Fiscal targets (2/2)

Is it time for a new set of fiscal targets?

- maybe not: no target better than a bad target?

But, perhaps, the Chancellor does have a target in mind?

- “always continuing to keep our debt falling”

Last two years of the forecast horizon see debt/GDP ratio falling by 1% of GDP a year

- low drop given small deficit; due to combination of low growth and loans not scored against the deficit

Borrowing an additional £15bn per year this would halve the reduction in debt/GDP ratio to 0.5% of GDP a year

Minor spending changes announced yesterday

Extra spending announced in response to higher expected inflation

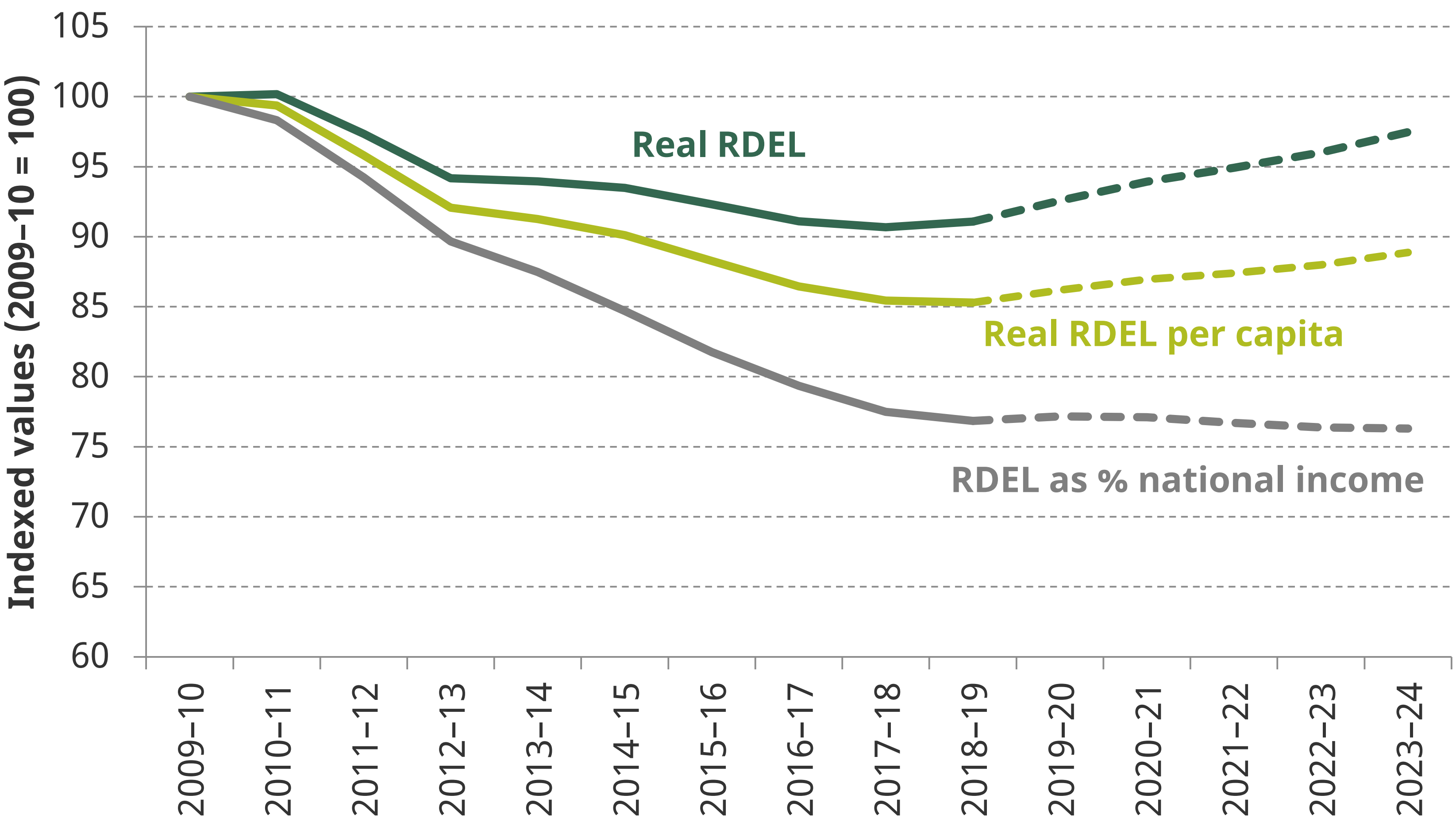
- extra £1.7 billion in 2023–24 relative to October plans
- £0.8 billion of which is for the NHS, to maintain £20.5 billion real increase agreed last summer

DHSC continues to shift money from capital to day-to-day budgets

- third year in a row this has been happened (£1.2 billion in 2016–17, £1.0 billion in 2017–18, £0.5 billion in 2018–19)

£1.6 billion 'Stronger Towns Fund' to be found entirely from existing spending totals in 2019–20 and 2020–21

Forecast change in day-to-day public service spending



Source: Author’s calculations using data from Office for Budget Responsibility *Economic and Fiscal Outlook.*

The forthcoming Spending Review

The Chancellor confirmed the Spending Review will cover the three years 2020–21, 2021–22 and 2022–23

- to be launched before summer recess and concluded alongside Budget

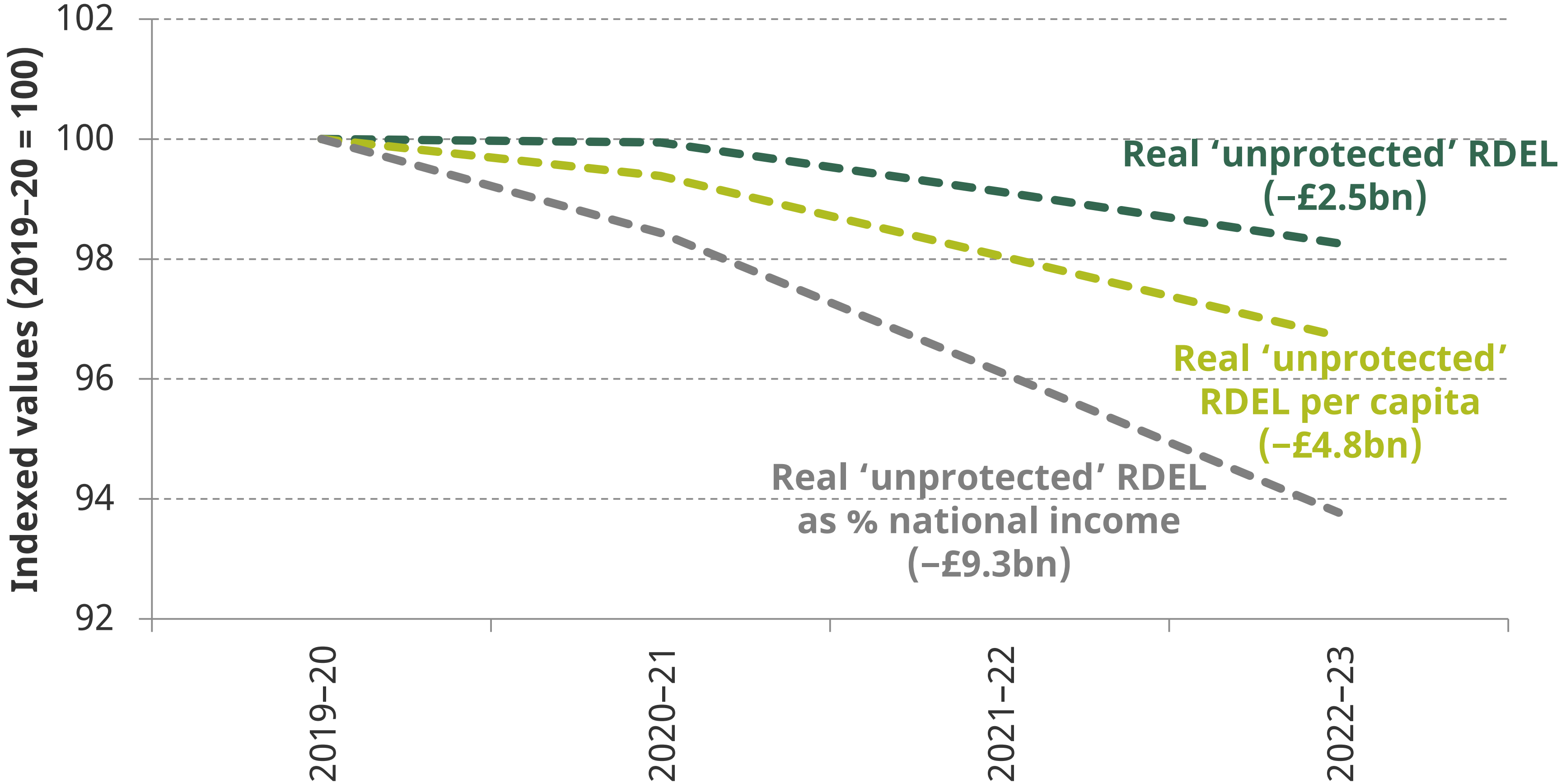
Several areas of spending are already protected

- NHS: day-to-day budget of NHS England to increase by £20.5 billion between 2018–19 and 2023–24
- Barnett formula implies extra money for Scotland, Wales and Northern Ireland
- defence: commitment to continue to spend at least 2% of GDP
- overseas aid: commitment to spend at least 0.7% of GNI

Together these comprise over half of day-to-day departmental spending

- current spending plans, combined with these commitments, imply cuts to unprotected departments

‘Unprotected’ day-to-day public service spending over the Spending Review period



Source: Author’s calculations using data from Office for Budget Responsibility *Economic and Fiscal Outlook.*

But could choose to spend more?

Unprotected areas are current facing cuts of 0.6% per year

- 1.1% per year in per capita terms
- on top of cuts of around 3% per year since 2010–11
- much slower pace of austerity, but still challenging

Pressures to increase spending on some ‘unprotected’ areas

- schools: freezing real per-pupil spending over the review period would cost around £1 billion extra by 2022–23
- many other spending pressures

Chancellor indicated he could decide to spend more

- indicated that an orderly EU exit could mean a boost to spending on public services: the so-called “deal dividend”

What if there was an extra £15 billion for public services?

Illustrative figure

Overall day-to-day spending would grow by 2.8% per year

- versus 1.2% per year on current plans

Still meet NHS and aid commitments…

… and increase defence and other unprotected budgets by 2.7% per year

- 2.2% per year in per capita terms, rising as a share of national income
- an end to austerity on public services any reasonable definition

What would that mean for borrowing?

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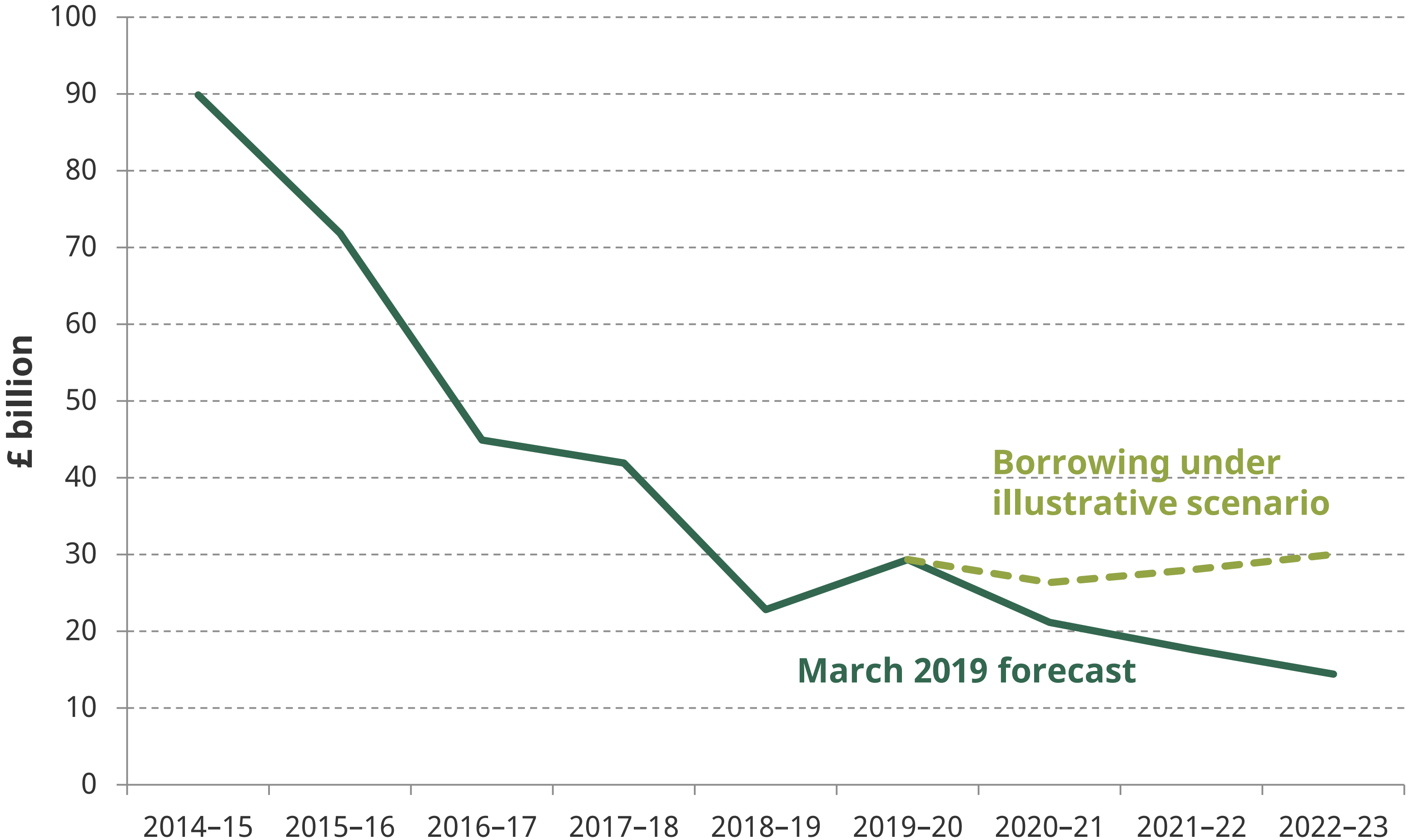

Source: Author's calculations using data from Office for Budget Responsibility *Economic and Fiscal Outlook.*

What if there was an extra £15 billion for public services?

Illustrative figure

- would certainly be a clear end to austerity on public services

Would keep forecast:

- borrowing below 2% of GDP, even after student loan accounting change
- debt ratio falling, though by just 0.5% of GDP a year towards end of forecast horizon

Relates to the public finance cost of Brexit so far:

- OBR revised down forecast receipts by £15 billion after referendum
- estimates that GDP around 2% lower than it would have been – for example from the BoE – suggest that, if anything, hit to receipts likely to have been greater

Conclusions

Modest increase in forecast receipts

- on top of a larger increase seen last Autumn

For now at least the Chancellor largely banked rather than spent the additional receipts

- provisional spending plans imply continued austerity for unprotected departments

Chancellor has headroom against his fiscal targets for this parliament, even after student loan accounting change

- could top up spending plans, end austerity for public services from March 2020, and still meet these fiscal targets
- but what about ambition to eliminate the deficit?