

The end of deficit reduction?

Thomas Pope

Some things didn't change yesterday

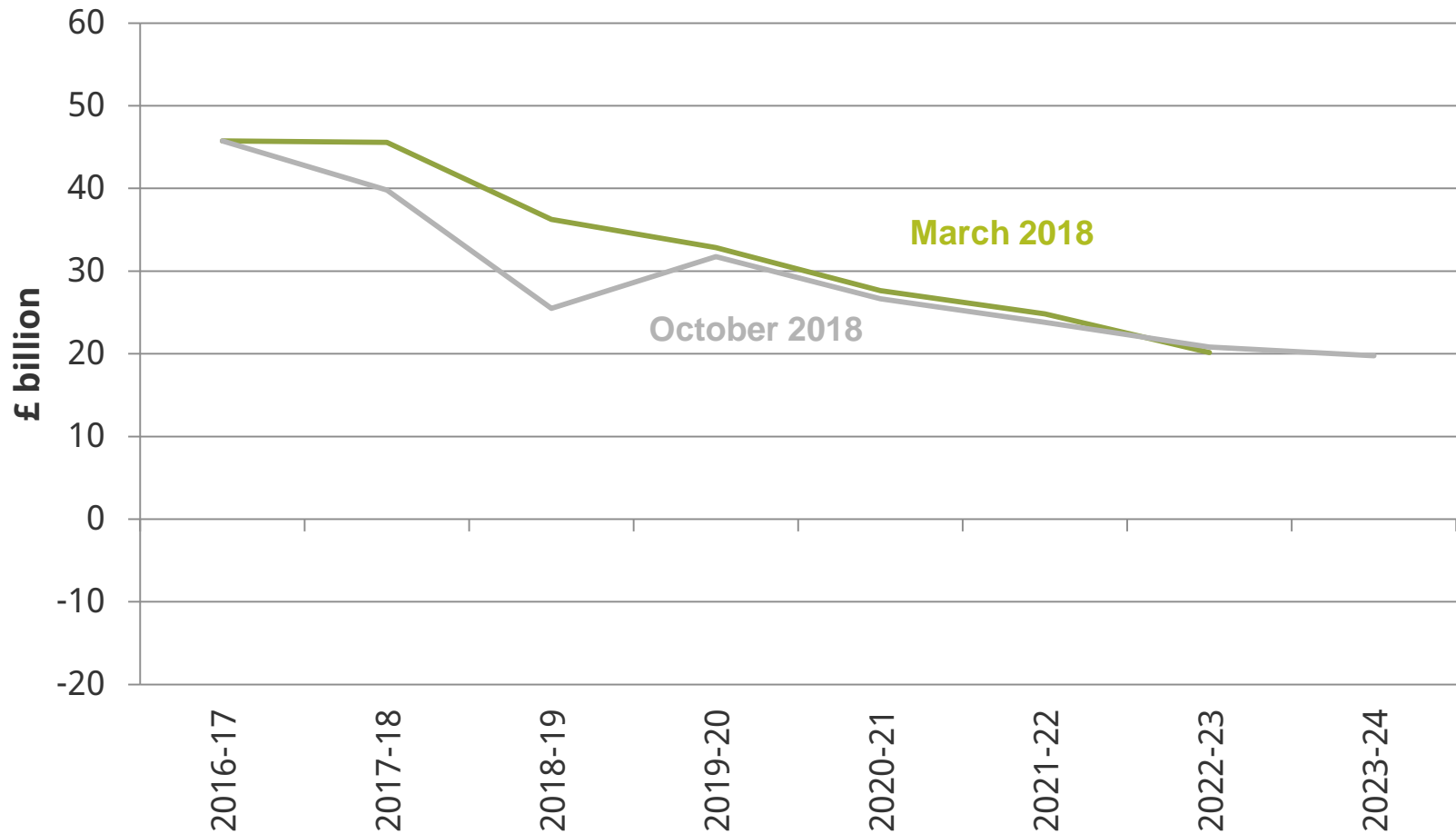
The medium-term growth forecast is still sluggish

- Real growth of only 1.6% forecast in 2023
- Pessimistic view of productivity remains
- Small improvement from better employment numbers

Medium-term borrowing forecast also virtually unchanged

- Borrowing of around £20 billion at the end of the forecast horizon

Successive forecasts for borrowing



Source: *Economic and Fiscal Outlook, October 2018*

A big underlying improvement

Table: changes to the deficit before effect of policy measures

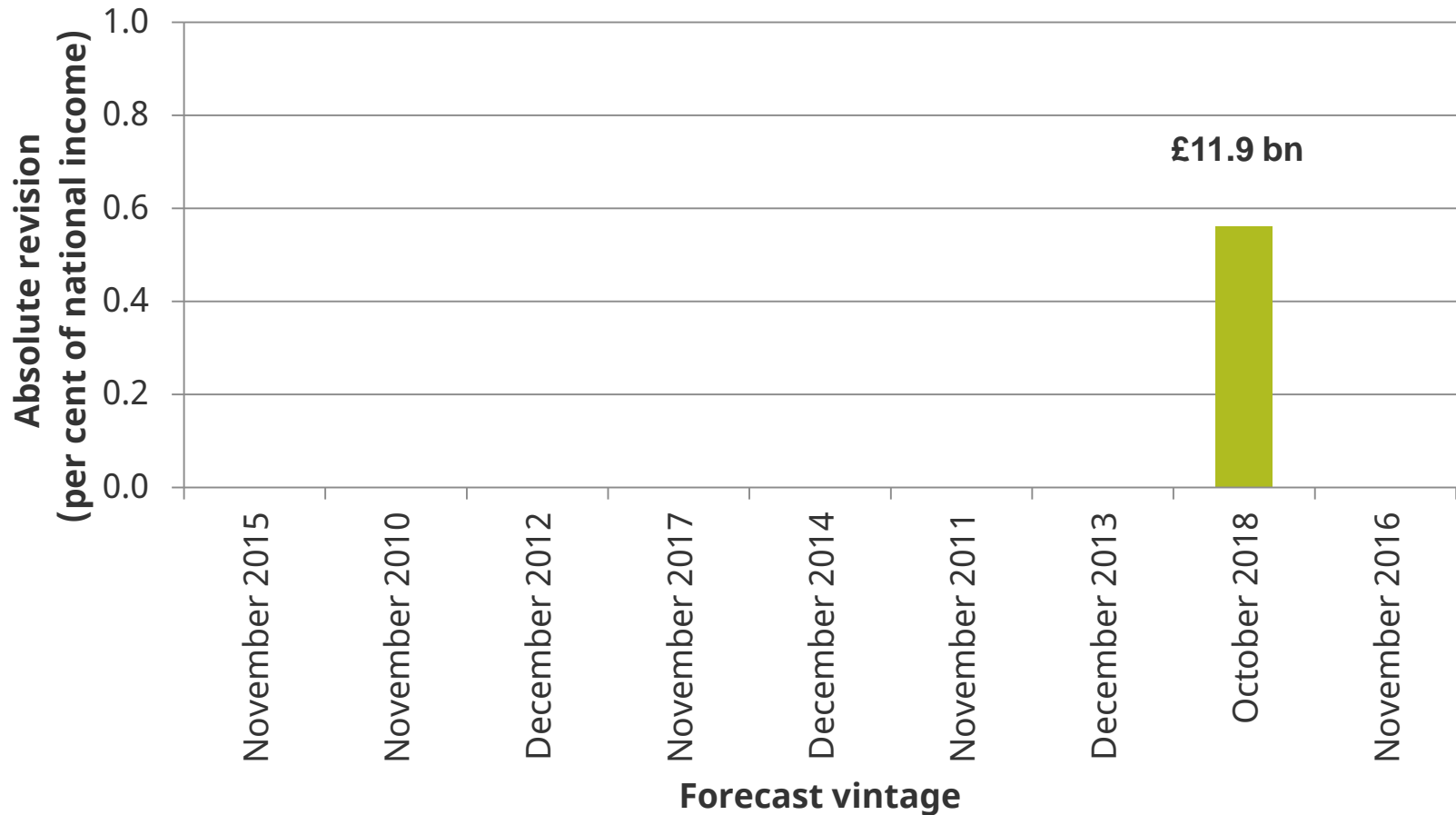
	2018–19	2019–20	2020–21	2021–22	2022–23
March forecast (restated)	36.2				
Higher receipts	-7.4				
<i>Of which</i>					
<i>Income tax & NICS</i>	-2.2				
<i>VAT</i>	-1.8				
<i>Corporation taxes</i>	-2.7				
<i>Other</i>	-0.8				
October forecast (pre-measures)	24.3				

A big underlying improvement

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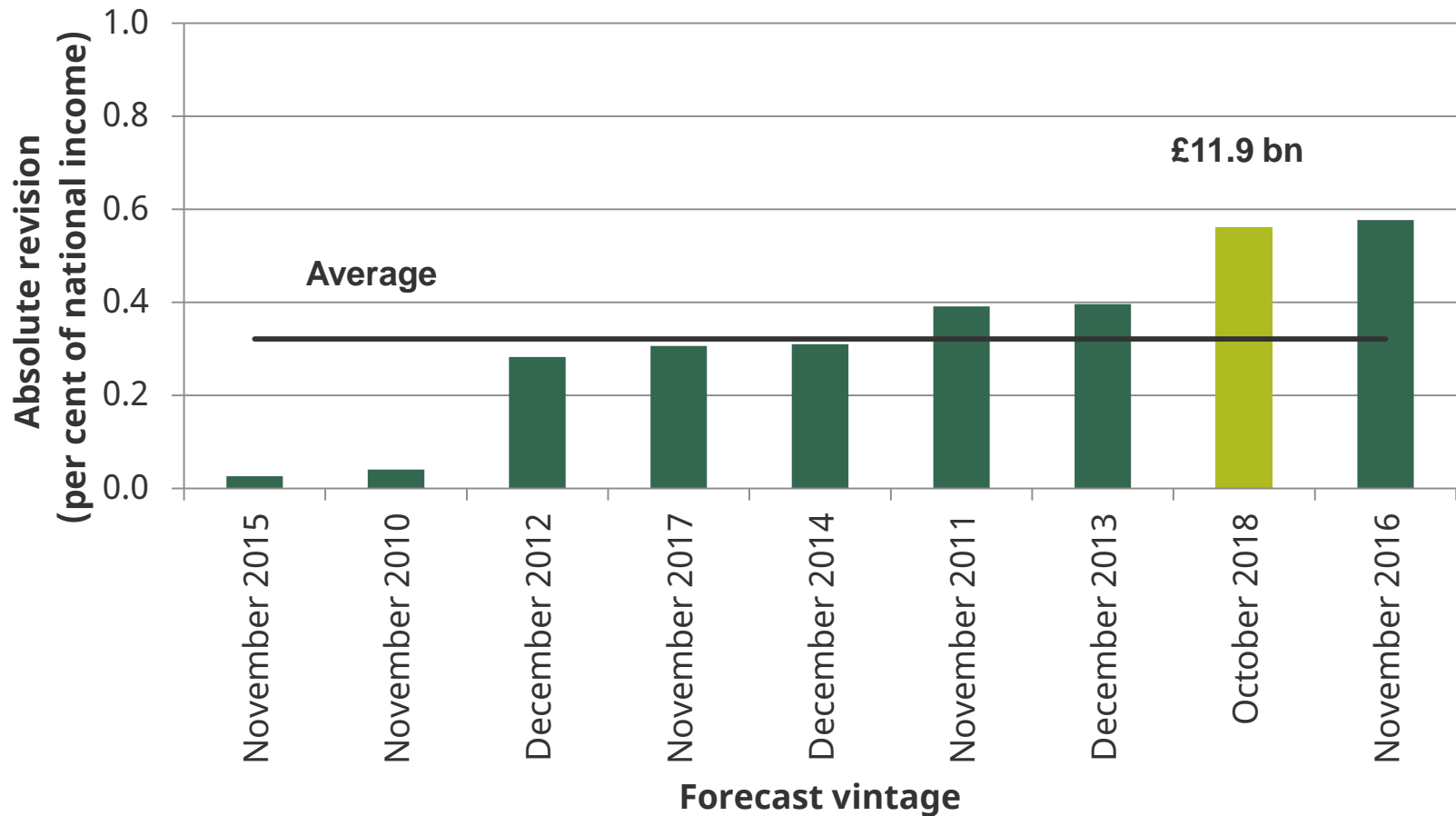
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Lower spending	-4.5				
Total underlying	-11.9				
October forecast (pre-measures)	24.3				

Second biggest Autumn in-year underlying revision since OBR began



Source: *Economic and Fiscal Outlook, October 2018*

Second biggest Autumn in-year underlying revision since OBR began

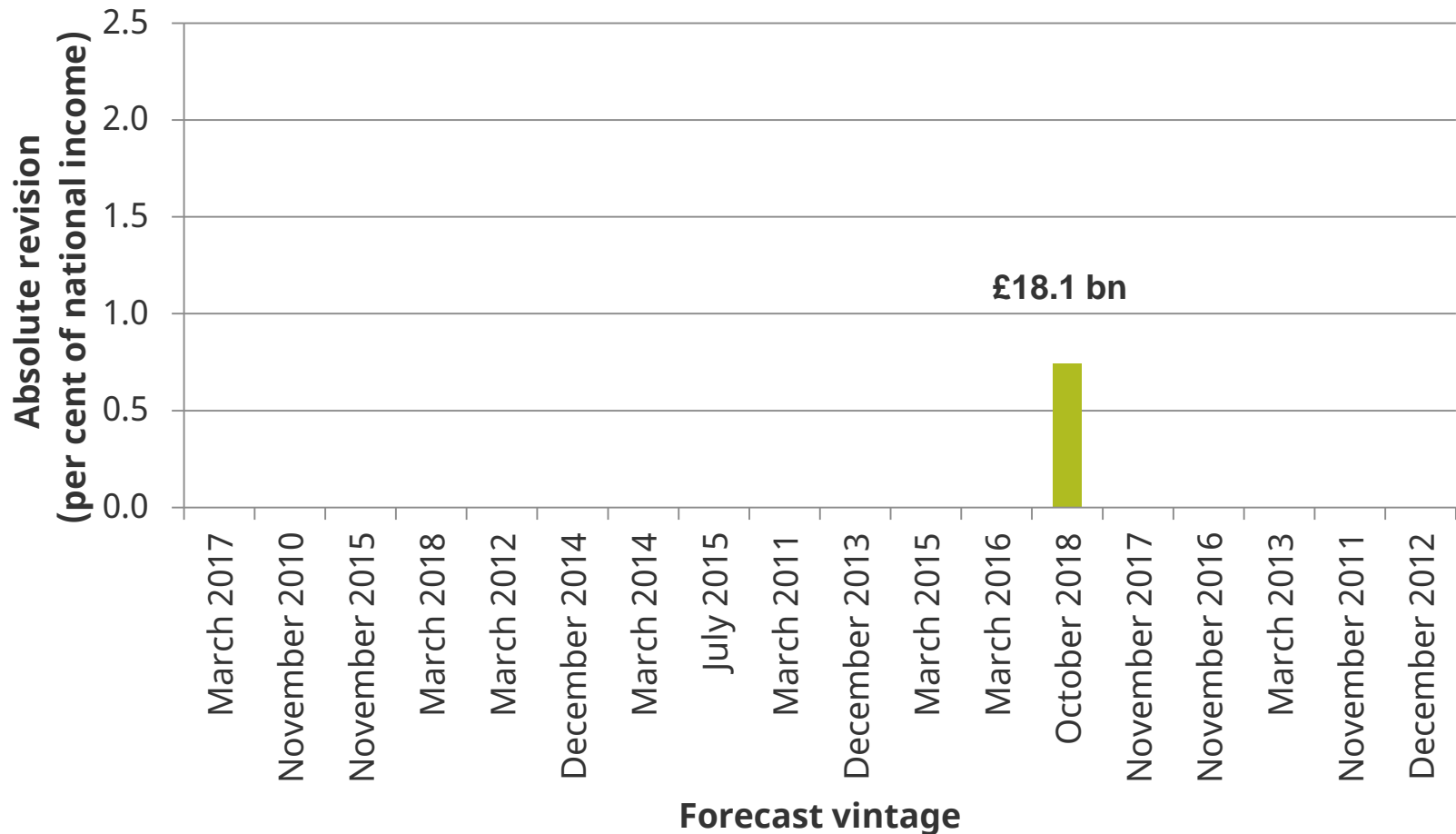


Source: *Economic and Fiscal Outlook, October 2018*

A big underlying improvement

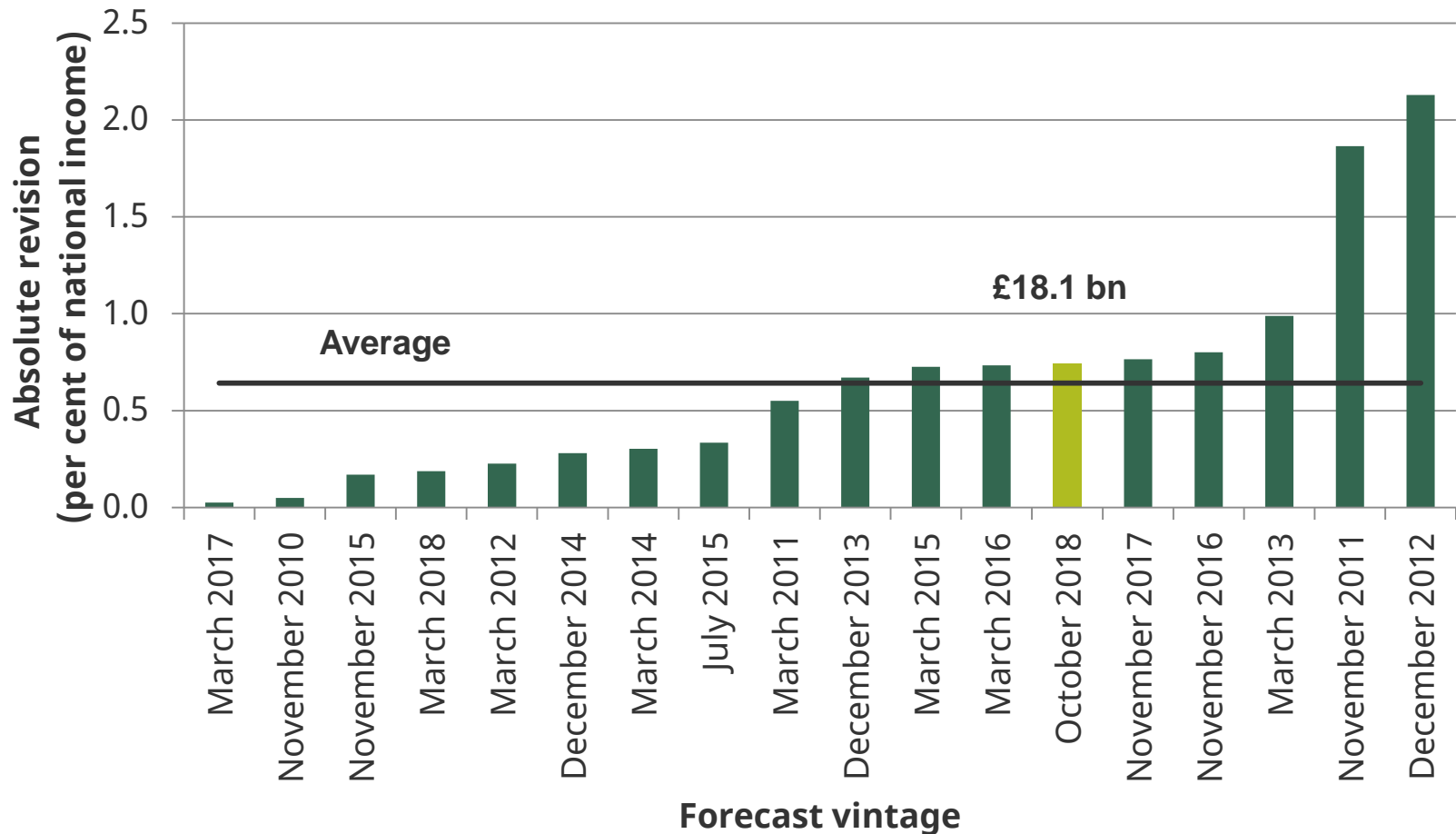
	2018–19	2019–20	2020–21	2021–22	2022–23
March forecast (restated)	36.2	32.9	27.6	24.8	20.2
Higher taxes	-7.4	-8.0	-8.0	-11.2	-14.1
<i>Of which</i>					
<i>Income tax & NICS</i>	-2.2	-0.3	-0.4	-1.1	-1.5
<i>VAT</i>	-1.8	-2.2	-2.5	-2.7	-2.7
<i>Corporation taxes</i>	-2.7	-3.6	-3.4	-4.5	-5.4
<i>Other</i>	-0.8	-1.8	-1.6	-2.9	-4.4
Lower spending	-4.5	-4.1	-3.7	-3.5	-4.1
Total underlying	-11.9	-12.0	-11.7	-14.7	-18.1
October forecast (pre-measures)	24.3	20.8	15.9	10.1	2.1

Sixth biggest final-year-of-forecast underlying revision since OBR began



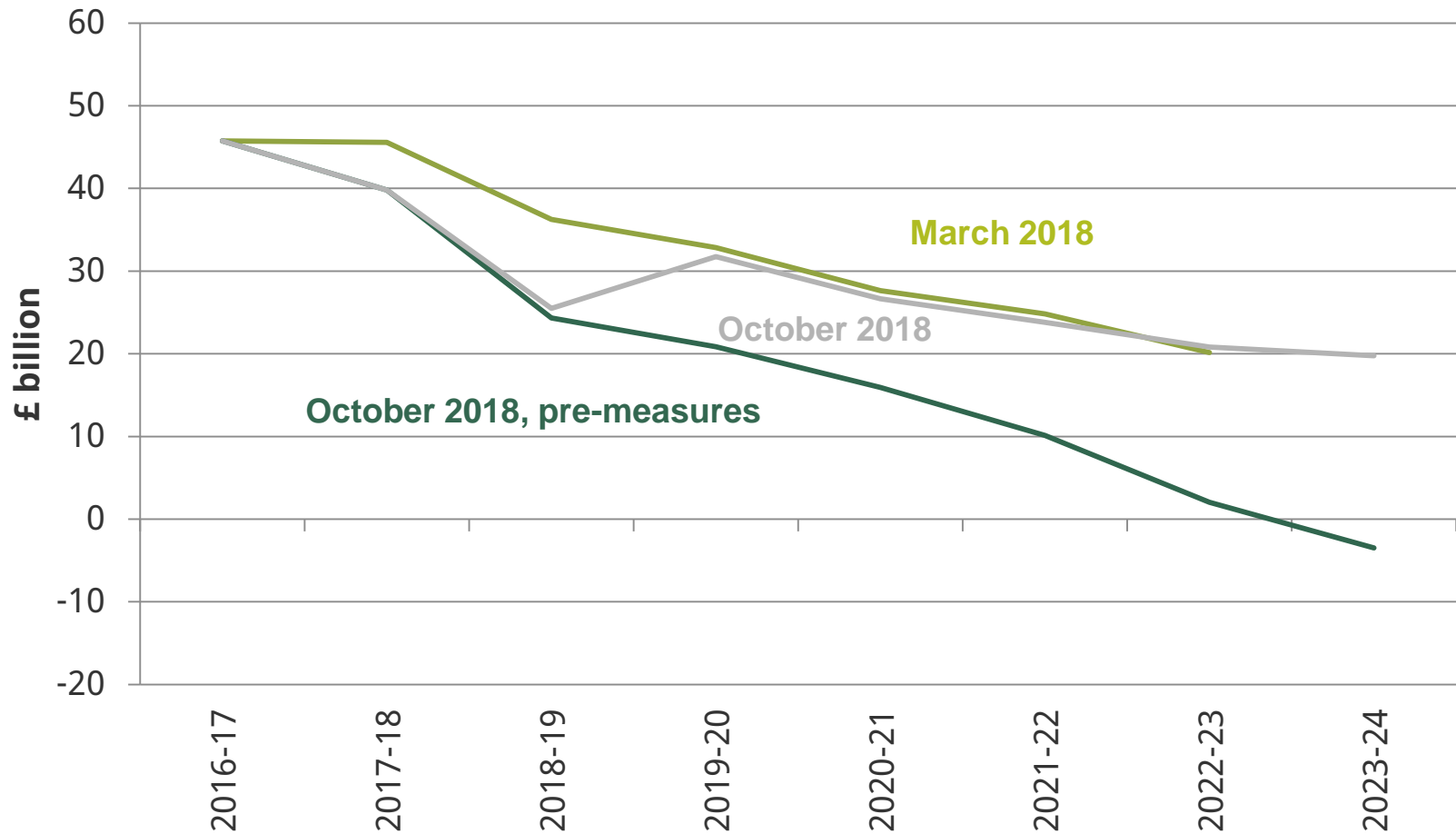
Source: OBR *Forecast revisions database*, *October 2018 Economic and Fiscal Outlook and Authors' calculations*

Sixth biggest final-year-of-forecast underlying revision since OBR began



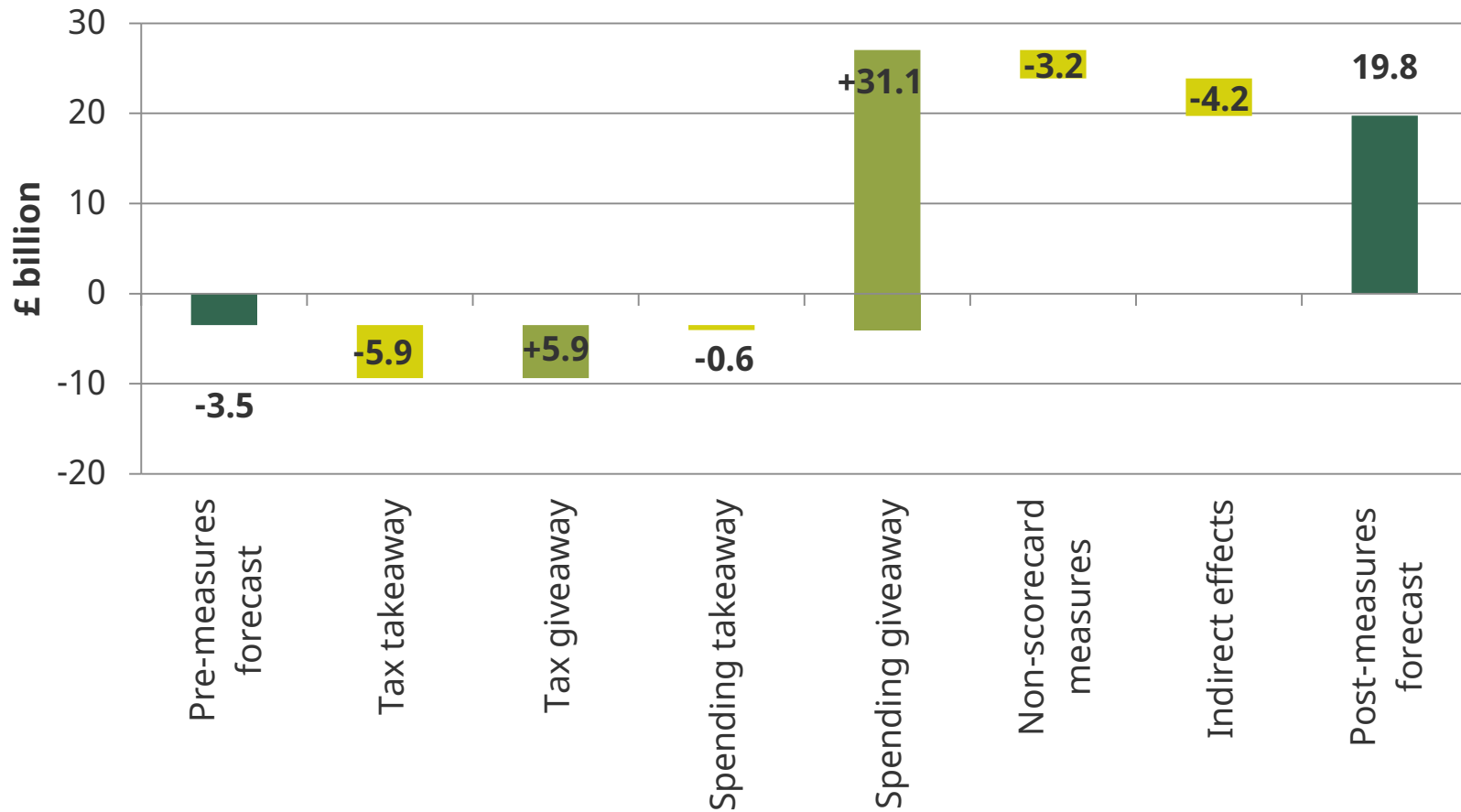
Source: OBR *Forecast revisions database*, *October 2018 Economic and Fiscal Outlook and Authors' calculations*

Successive forecasts for borrowing



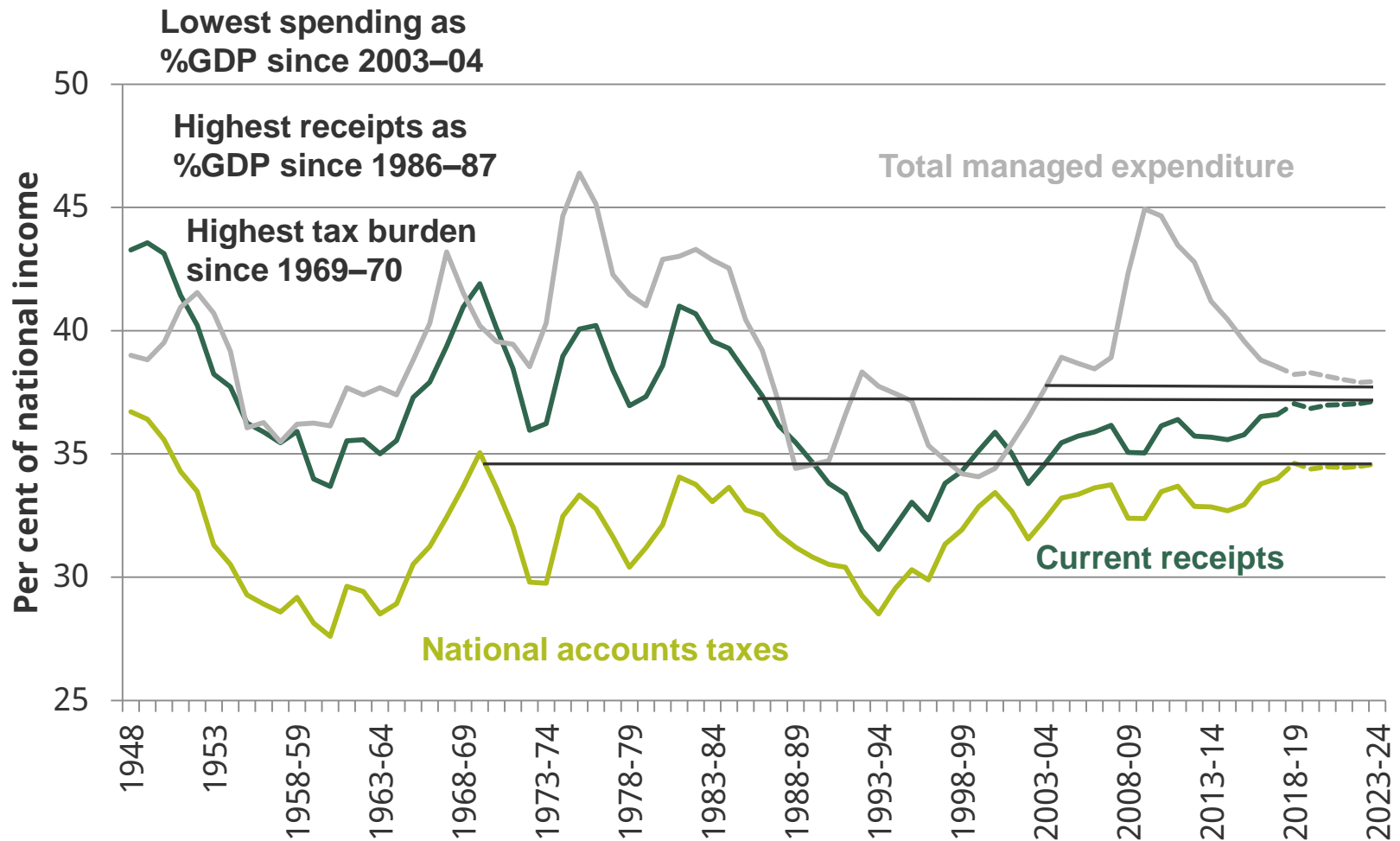
Source: *Economic and Fiscal Outlook, October 2018*

Effects of budget policy measures on borrowing, 2023-24



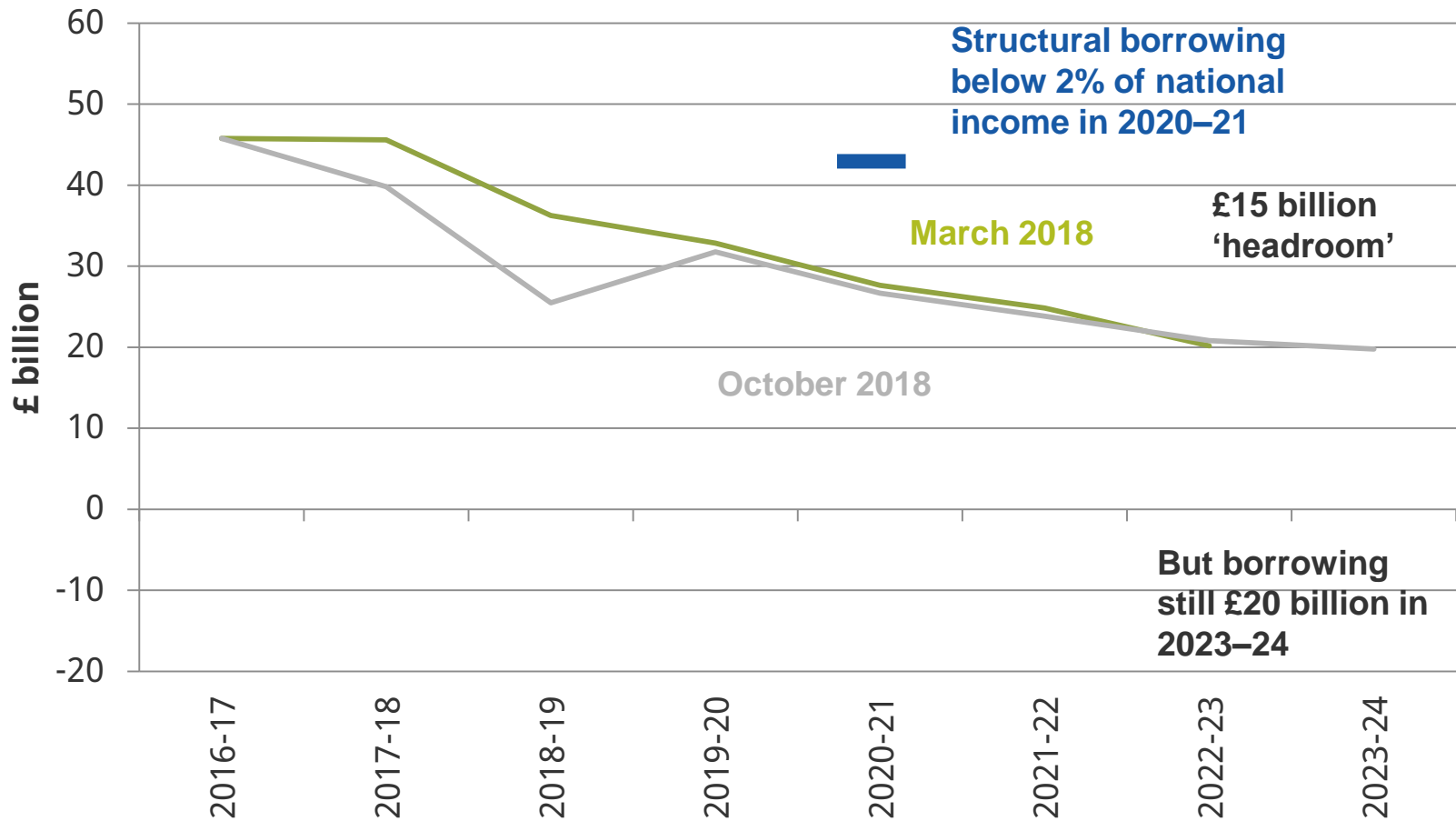
Source: *Economic and Fiscal Outlook, October 2018*

What this means for aggregate tax and spend



Source: OBR Databank, October 2018

Headroom against 2020–21 borrowing target



Source: *Economic and Fiscal Outlook, October 2018*

A double “deal dividend”?

1) “£15.4bn headroom against our 2% Fiscal Rules target”

- True of 2020–21 deficit target
- But deficit of £20 billion forecast for 2023–24 despite overarching objective to eliminate the deficit by the mid-2020s

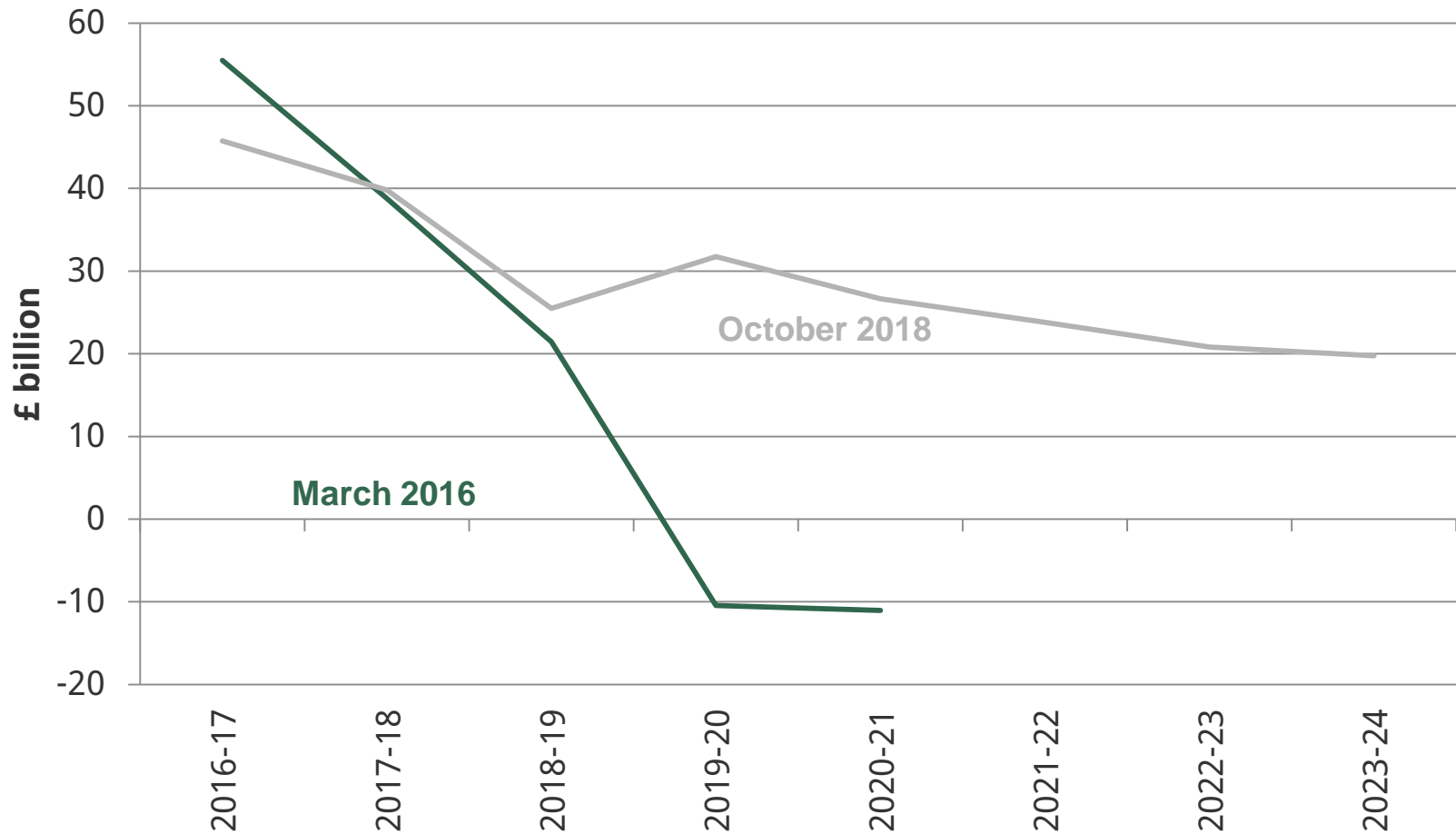
2) Better-than-expected deal signed with the EU, uncertainty reduced

- Likely boost to forecast growth and revenues, reducing some of the forecast £15 billion hit to revenues in 2020–21
- But a worse-than-expected deal – or no deal – would be likely to reduce forecast growth and revenues

3) The UK's net financial contribution to the EU Budget, net of spending done by the EU in the UK or on our behalf

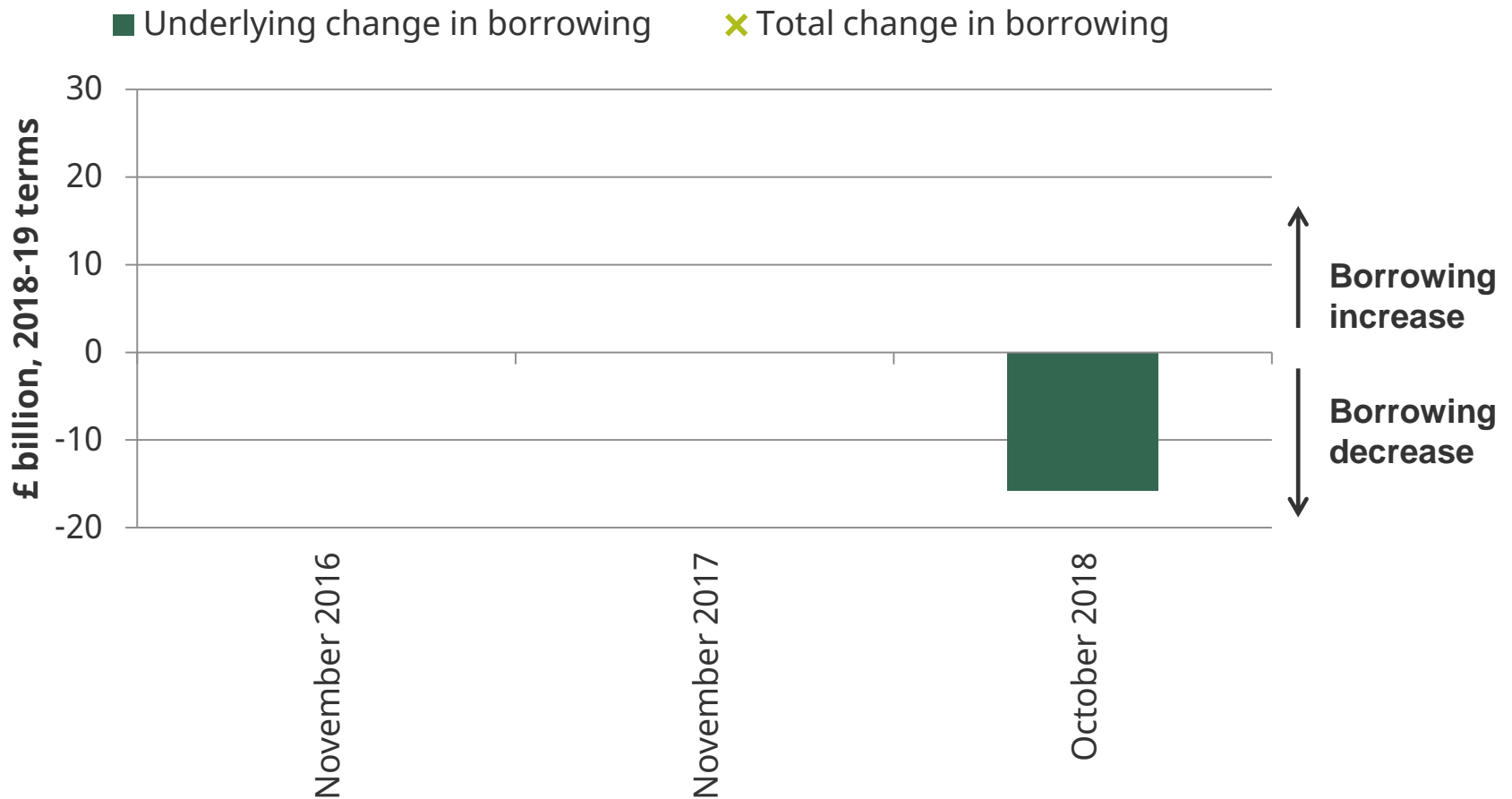
- Won't deliver saving over next Spending Review period due to “divorce settlement” and meeting additional costs to public services from Brexit

Borrowing from next year higher than pre-referendum forecasts



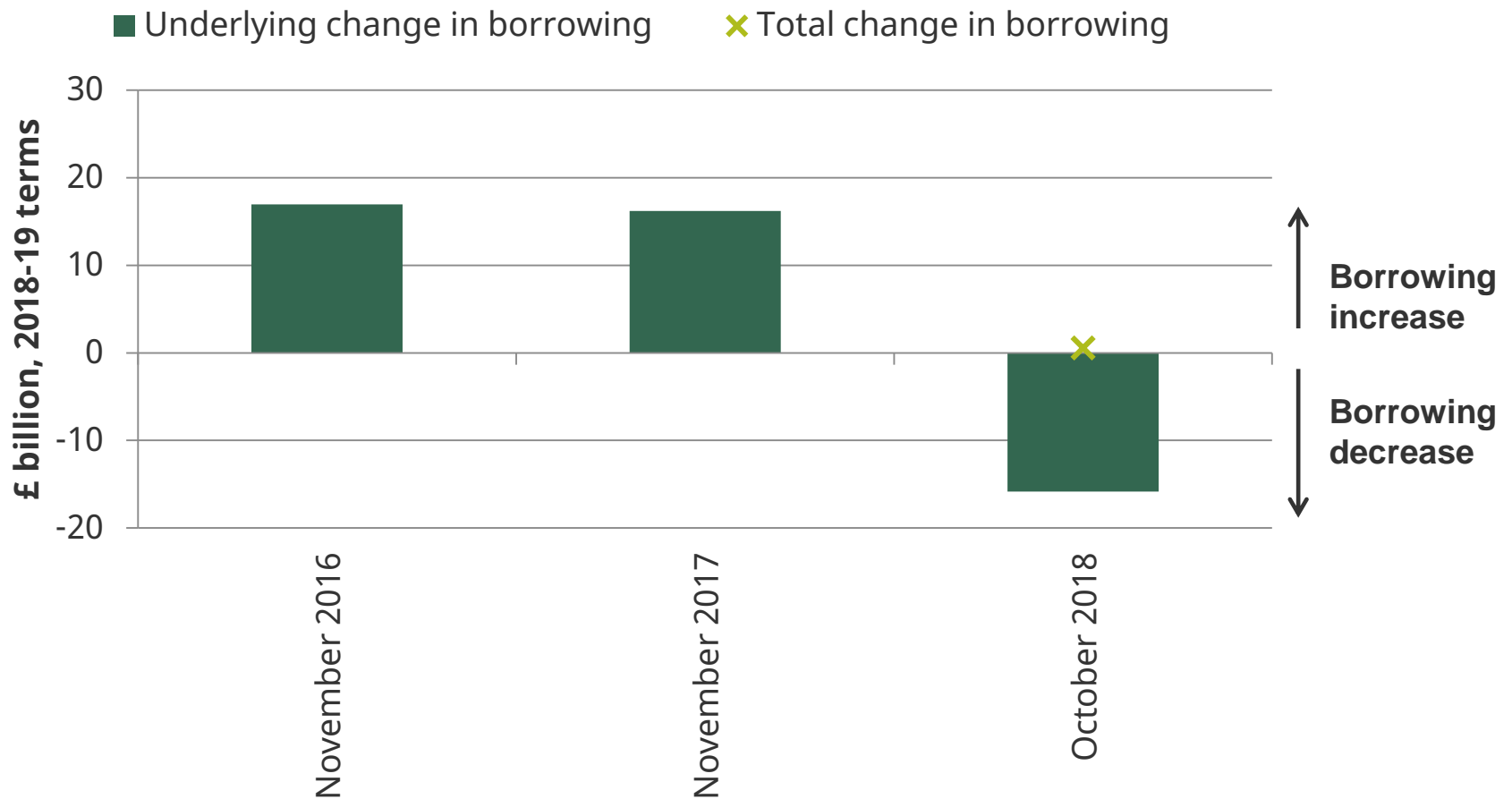
Source: *Economic and Fiscal Outlook, March 2016 & October 2018*

An unbalanced approach



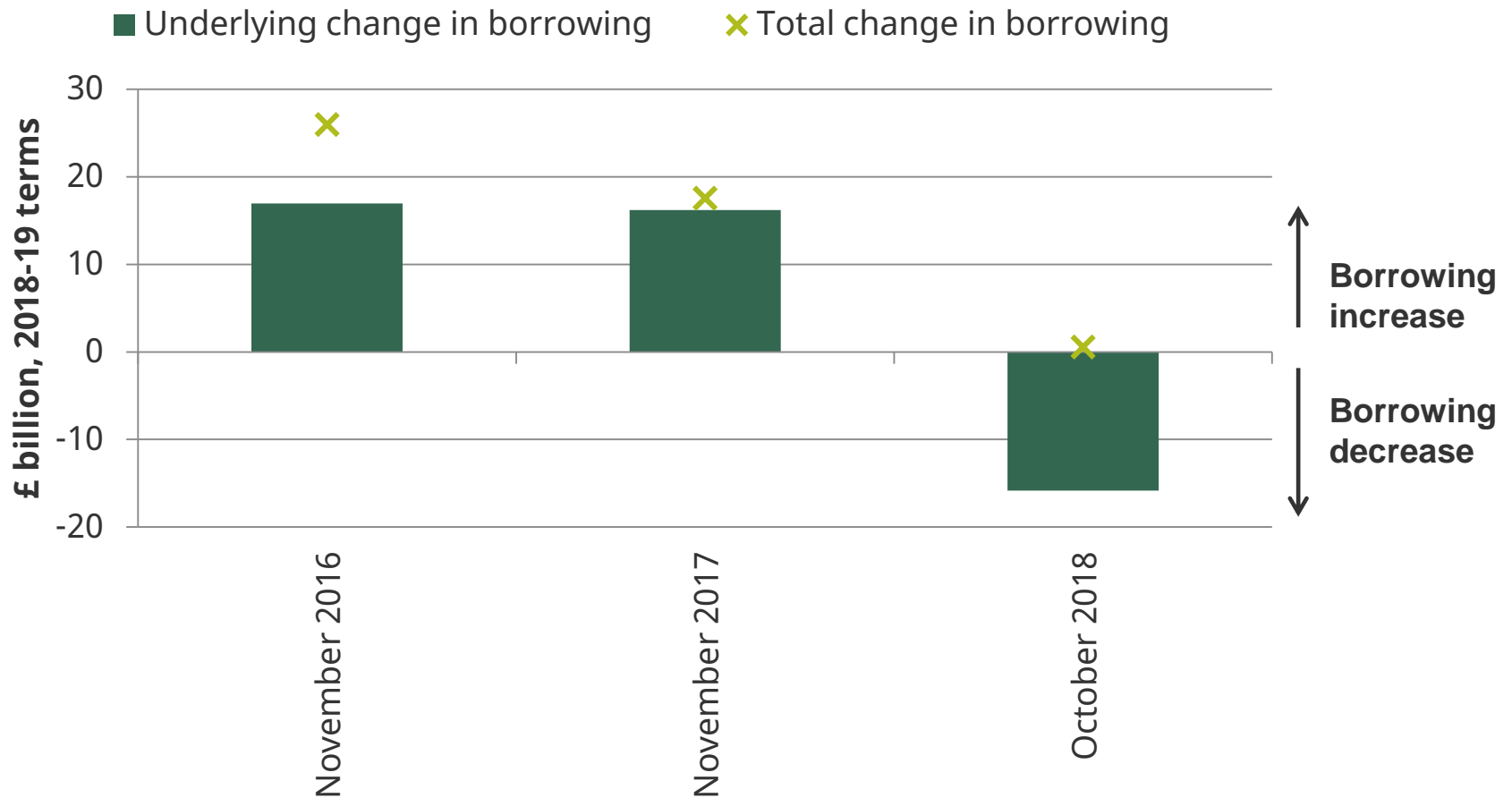
Source: OBR *Forecast Revisions Database* and *Economic and Fiscal Outlook*, October 2018

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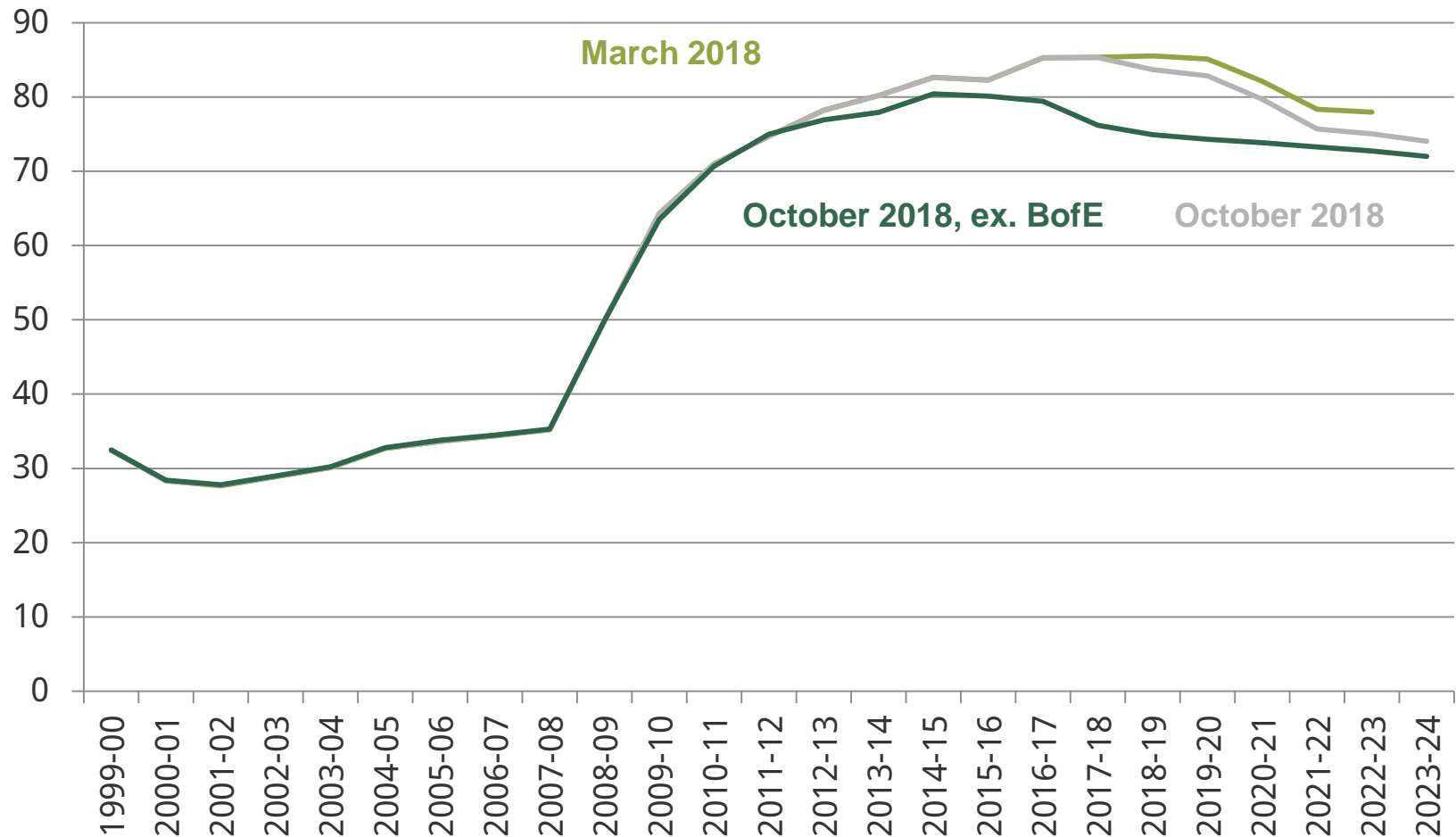
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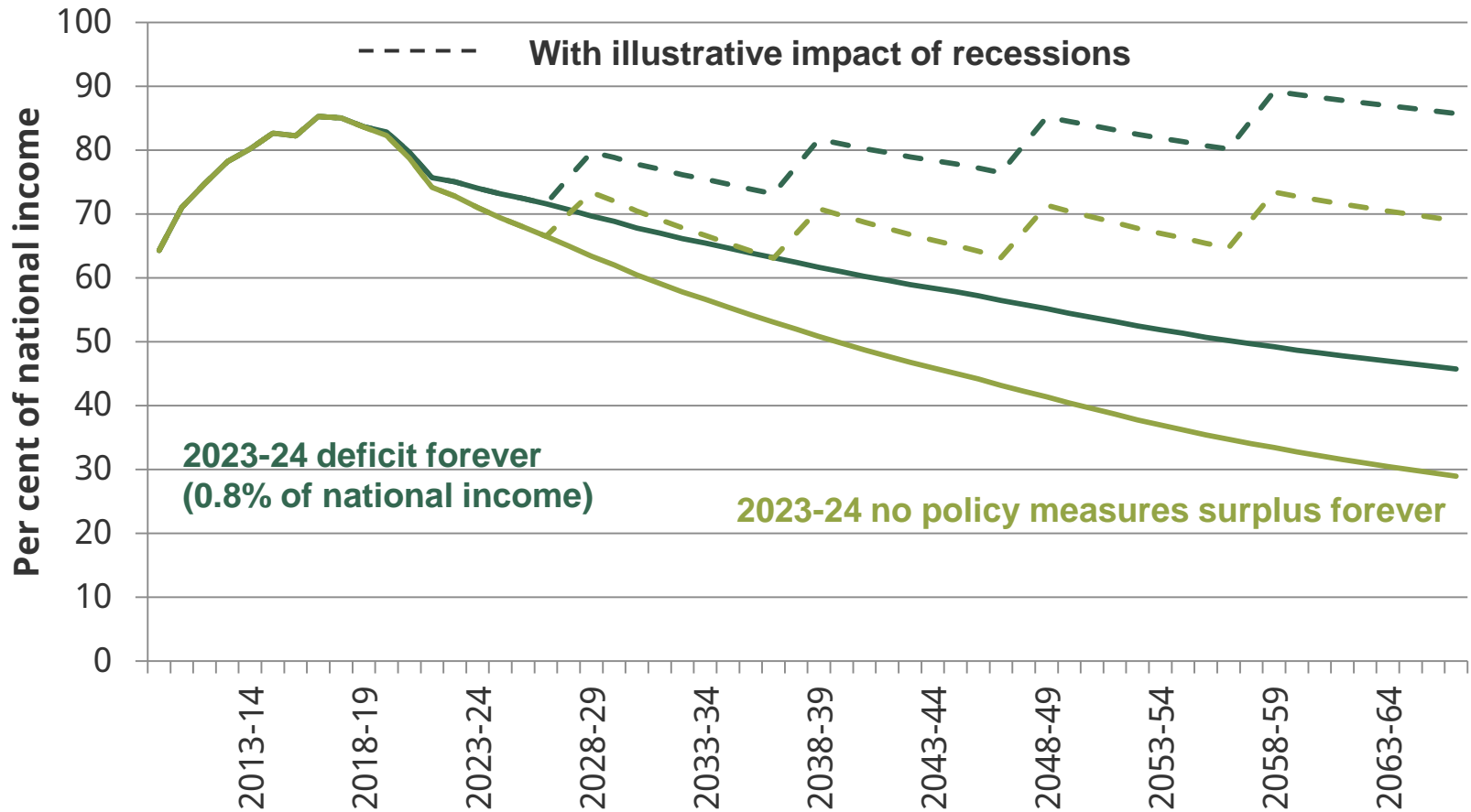
Source: OBR *Forecast Revisions Database* and *Economic and Fiscal Outlook*, October 2018

Debt still much higher than pre-crisis levels and falling slowly



Constant deficit beyond 2023-24 not cost-free

Figure: Paths for the long-run debt



Source: Authors' calculations using *Economic and Fiscal Outlook, October 2018* and *Fiscal Sustainability Report 2018*

Summary

A substantial forecast improvement

- Despite a broadly unchanged economic forecast
- Strong public finances this year assumed to persist over medium term

Chancellor spent all of this forecast improvement

- Mainly on higher NHS spending
- With the possibility of more spending in the event of a 'good deal'
- Chancellor continues pattern of responding differently to forecast improvements and deteriorations

Further consolidation still required to eliminate the deficit

- Seems likely that this target will not be met