United Kingdom

Country note, January 2019

Office for Budget Responsibility

Key messages:

- We forecast real GDP growth of 1.6 per cent in 2019, falling back to 1.4 per cent in 2020 and 1.4 per cent in 2020.
- We expect public sector borrowing of £25.5 billion in 2018-19 (1.2 per cent of GDP), falling gradually to £19.8 billion in 2023-24.
- The Government is on course to meet its three fiscal targets on the basis of our latest central forecast.
- Its 'fiscal objective' to balance the budget by the middle of the next decade looks more challenging.
- Our forecasts are based on broad-brush assumptions regarding the UK's exit from the EU, rather than a specific outcome.

Macroeconomic outlook

The performance of the real economy has been less impressive relative to expectations. We have revised real GDP growth in 2018 down from 1.5 to 1.3 per cent, but primarily due to the temporary effects of the snowy first quarter. Thereafter we expect slightly stronger growth over the forecast as a whole than in our previous forecast in March, reflecting a downward revision to our estimate of the sustainable rate of unemployment and an upward revision to potential labour market participation, reflecting new data on participation by age.

Short-term fiscal outlook

Public sector net borrowing has fallen from its post-crisis peak of 9.9 per cent of GDP (£153.1 billion) in 2009-10 to 1.2 per cent of GDP (£25.5 billion) in 2018-19. With economy running a little above potential, we judge that the 2018-19 structural deficit (which excludes the effect of the economic cycle) is close to the headline deficit at 1.3 per cent of GDP. The deficit is expected to rise by around £6 billion in 2019-20.

Medium-term fiscal outlook

We expect the deficit increase slightly in 2019-20 to 1.4 per cent of GDP but fall slowly over the four years to 2023-24. Our central forecast is for a structural deficit of 1.3 per cent or GDP in 2020-21, below the 2 per cent of GDP ceiling set in the Government's 'fiscal mandate'. We expect debt to fall as a share of GDP over the forecast period from 83.7 per cent of GDP in 2018-19 to 74.1 per cent.

Fiscal framework and national fiscal rules

The Government has set itself three fiscal rules that require:

- the structural deficit (cyclically adjusted public sector net borrowing) to be below 2 per cent of GDP by 2020-21;
- public sector net debt to fall as a percentage of GDP in 2020-21; and
- welfare spending (excluding the state pension and payments closely linked to the economic cycle) to be below a welfare cap that was set for 2022-23, in line with our November 2017 forecast for that year.

Our latest central forecast shows all three targets on course to be met, with the deficit target met by a margin of 0.7 per cent of GDP. The Government's longer-term aim of balancing the public finances by the middle of the next decade looks more challenging, as the pace of deficit reduction slows towards the end of the forecast and as age-related pressures on the public finances are set to mount. Had there been no fiscal loosening in the October 2018 Budget, the objective would have been achieved in 2023-24.

Key indicator forecast

Forecasts and charts all from the October 2018 *Economic and fiscal outlook*.

	Forecast					
	2018-19	2019-20	2020-21	2021-22	2022-23	2022-24
Real GDP (% change year-on-year, calendar year)	1.3	1.6	1.4	1.4	1.5	1.6
Output gap (per cent of potential output)	0.3	0.3	0.2	0.1	0.1	0.1
Public sector net borrowing (% of GDP)	1.2	1.4	1.2	1.0	0.9	0.8
Cyclically adjusted net borrowing (% of GDP)	1.3	1.6	1.3	1.1	0.9	0.8
Public sector net debt (% of GDP)	83.7	82.8	79.7	75.7	75.0	74.1
Real public spending (% change year-on-year)	0.6	1.7	1.1	1.1	1.2	1.7

Chart 1: Real GDP fan chart

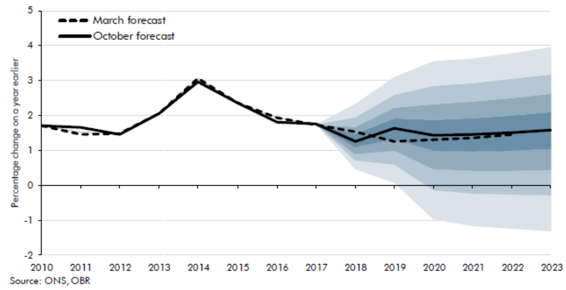


Chart 2: Public sector net borrowing

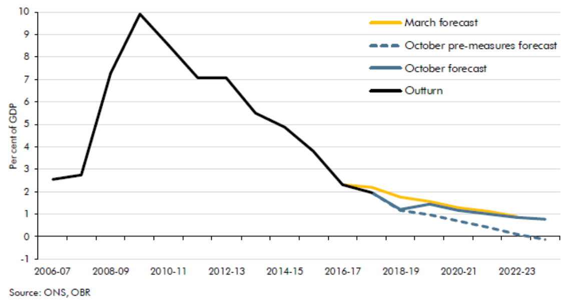
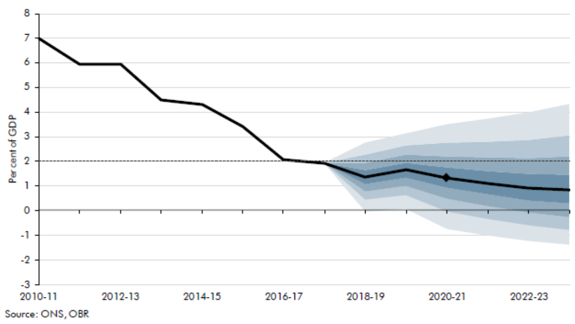


Chart 3: Cyclically adjusted public sector net borrowing fan chart



Mark.Dembowicz@obr.uk obr.uk +44 203 334 6101