HM Treasury

# 2019-20 Convergence Programme for the United Kingdom:

## submitted in line with the Stability and Growth pact

April 2020

© Crown copyright 2020

This publication is licensed under the terms of the Open Government Licence v3.0 except where otherwise stated. To view this licence, visit nationalarchives.gov.uk/doc/open-government-licence/version/3.

Where we have identified any third-party copyright information you will need to obtain permission from the copyright holders concerned.

This publication is available at: www.gov.uk/official-documents.

Any enquiries regarding this publication should be sent to us at public.enquiries@hmtreasury.gov.uk

ISBN 978-1-913635-28-2

PU 2966

# Contents


| | | |
|---|---|---|
| Foreword | | 2 |
| Chapter 1 | Introduction | 4 |
| Chapter 2 | Overall policy framework and objectives | 5 |
| Chapter 3 | Quality of public finances | 98 |
| Chapter 4 | Institutional features of public finances | 103 |
| Annex A | OBR analysis | 106 |
| Annex B | Fiscal impact of policy decisions | 274 |
| Annex C | Supplementary data tables | 281 |

# Foreword

Since the publication of the Budget and the accompanying OBR forecast it has become clear that the UK, along with the rest of the world, is facing significant economic disruption in the wake of the Covid-19 pandemic. The government's careful management of the public finances means that it is well placed to deal with the challenges posed by Covid-19. The government has announced unprecedented support for businesses and workers to protect them against the current economic emergency caused by the Covid-19 outbreak.

The global economy has been hit hard by the spread of Covid-19 and the accompanying containment measures. Early data releases suggest the short-term impact of Covid-19 on the global economy may be significantly larger than that of the global financial crisis.

The UK is facing significant economic disruption, but the underlying causes of this disruption will pass. The spread of the virus means that growth in 2020 is going to be significantly below that of last year, though estimates are highly uncertain. This is why the government has acted to support people and businesses, to minimise deep and long-lasting impacts, and to support the economy through this difficult period. The economic support that is being offered is unprecedented. However, the consensus both in the government and among external economists is that not taking these steps would risk the effects of the Covid-19 virus leaving permanent scars on our economy. The independent OBR have said that "the costs of inaction would certainly have been higher".

Spring Budget 2020 was delivered to meet the following fiscal rules:

- to have the current budget at least in balance by the third year of the rolling, five-year forecast period
- to ensure that public sector net investment (PSNI) does not exceed 3% of GDP on average over the rolling five-year forecast period
- if the debt interest to revenue ratio is forecast to remain over 6% for a sustained period, the government will take action to ensure the debt-to-GDP ratio is falling

The Office for Budget Responsibility's (OBR) Budget forecast confirmed that the government delivered the budget within these fiscal rules.

The government made significant progress since 2010 in restoring the public finances to health; by 2018-19 the deficit had been reduced by four-fifths – from 10.2% of GDP to 1.8% – and debt brought back under control. The work of the last ten years in bringing borrowing and debt back under control has ensured the public finances are well placed to deal with the challenges posed by Covid-19.

However, it is clear that the impact on the economy as a result of Covid-19, and the government's necessary response to it, will lead to a significant increase in borrowing this year compared to the OBR's forecast. We expect this increase in borrowing to be

temporary. Under the OBR's Covid-19 reference scenario[1] borrowing is expected to rise sharply this year, but fall back quickly in 2021-22 as temporary policy costs end and the economy recovers. The OBR note that the government's policy response will have substantial direct fiscal costs, but that the measures taken should help limit the long-term damage to the economy and public finances – and the costs of inaction would have been higher.

[1] Coronavirus reference scenario, OBR, April 2020

# Chapter 1 Introduction

The Stability and Growth Pact (SGP) requires Member States to provide information on economic developments in their country for the purposes of the multilateral surveillance procedure under Articles 121 and 126 of the EU Treaty. Member States submit either annual Stability Programmes (euro area countries) or annual Convergence Programmes (non euro area countries) setting out their medium-term fiscal policies.

On 31 January 2020, the United Kingdom withdrew from the European Union. As set out in the Withdrawal Agreement, the United Kingdom will continue to apply the EU acquis, including in matters relating to the European Semester and the Stability and Growth Pact (SGP), for the duration of the transition. Therefore, during this period the government continues to submit its Convergence Programme.

The UK cannot face sanctions under the SGP. The UK's obligation under the SGP is to "endeavour to avoid an excessive government deficit" as a result of its Protocol to the EU Treaties (Protocol 15). The Convergence Programme sets out the UK's medium-term fiscal policies.

The Spring Budget 2020 has been the only major fiscal event since the last Convergence Programme. The Convergence Programme 2020 draws largely from the announcements of this publication.

The forecasts for the economy and public finances included in the UK's Convergence Programme are prepared by the independent Office for Budget Responsibility (OBR). Information on the OBR's mandate is set out in Chapter 4. The forecasts set out in the Convergence Programme are from the OBR's March 2020 Economic and Fiscal Outlook, which was published alongside Spring Budget 2020.

Under Section 5 of the European Communities (Amendment) Act 1993, Parliament is required to approve the government's assessment of the UK's medium-term economic and budgetary position. This forms the basis of the UK's Convergence Programme. The UK presents copies of assessments of its Convergence Programme to Parliament.

## Structure of the Convergence Programme

The first five chapters of this Convergence Programme set out the government's policy on the fiscal position, sustainability of the public finances and the macro-economy, as required by the Stability and Growth Pact Code of Conduct.

Detail on the OBR's economic and fiscal forecasts is set out separately in Annex A of the Convergence Programme, drawing upon the OBR's March 2020 Economic and Fiscal Outlook Annex B provides details of the financial impact of Spring Budget 2020 policy decisions. Annex C provides supplementary data.

Annex B provides details of the financial impact of Spring Budget 2020 policy decisions. Annex C provides supplementary data

# Chapter 2
# Overall policy framework and objectives

The government published a Budget on 11 March 2020. To fulfil their legal requirements to publish two forecasts per year, the Office for Budget Responsibility (OBR) also published a second supplementary forecast in March.

The following chapters are from the Budget 2020 document. Please note that where these chapters reference the OBR forecast, they refer to the 11 March 2020 forecast.

# 1 Budget Report

## Economy and Public Finances

**1.1** The UK economy has many strengths: a globally competitive tax system, some of the best universities in the world, is home to many highly innovative firms, and its economic prospects are underpinned by a strong macroeconomic framework. Since 2010, the economy has grown faster than France, Italy and Japan. Employment is at a record high and the unemployment rate is the joint-lowest since 1975. In common with other advanced economies, the UK faces economic challenges. In the near term, the outbreak of COVID-19 is expected to have a significant but temporary effect on the economic outlook. Productivity remains weak and is distributed unevenly across the country; and the transition to a net zero economy by 2050 will require radical changes in every sector.

**1.2** The Budget announces a plan to support the economy over the short term in response to the COVID-19 outbreak. This includes measures to support public services, individuals and businesses.

**1.3** The Budget builds on the UK's economic strengths and takes steps to address the UK's long-standing structural challenges. The government is committed to levelling up across the UK in order to raise productivity and growth in all nations and regions, creating opportunity for everyone and addressing disparities in economic and social outcomes.

**1.4** Since 2010, the government has restored the public finances to health after inheriting debt that had nearly doubled in two years. The deficit has been reduced by four fifths from a post-war peak of 10.2%[1] of GDP in 2009-10 to 1.8% of GDP in 2018-19.

**1.5** With historically low borrowing costs and the public finances in a more secure position, the government can now increase borrowing for investment without compromising fiscal sustainability. The Budget provides significant levels of funding for public services to meet the economic challenges and priorities of today, and to address the long-term challenge of low productivity growth.

**1.6** This increase in spending, which provides the envelope for the upcoming CSR, has been delivered while meeting a set of fiscal rules that ensures the government is only borrowing to invest over the medium term, with the current budget in surplus, and that limits public sector net investment to an average of 3% of GDP, to keep control of borrowing and debt. To ensure the fiscal framework remains appropriate for the current macroeconomic environment HM Treasury will undertake a review over the summer and announce any changes by Autumn Budget 2020.

[1] Details of the sources of all numerical references, including National Statistics, used in this section can be found in 'Spring Budget 2020 data sources'.

## Economic context

**1.7** The OBR's economy forecast was closed for new data when the spread of COVID-19 was at a much earlier stage. As such, the OBR's forecast includes an estimate of the impact on global growth, based on the assumption that the spread of the virus would be relatively limited. The forecast does not reflect the now global spread of COVID-19 or an outbreak in the UK.

## Global economy

**1.8** The International Monetary Fund (IMF) estimates that the global economy grew by 2.9% in 2019, down from 3.6% in 2018, and the slowest growth since the financial crisis (Chart 1). The COVID-19 outbreak is expected to reduce global growth this year. The OBR forecasts that annual global GDP growth will be 3.0% in 2020, down from 3.6% in its Spring Statement 2019 forecast. This includes an assumption that the outbreak would be "relatively limited" and its impact on the forecast "largely confined to a modestly weaker outlook for growth in world trade and the UK's export markets." The OBR notes that, since closing its global forecast to new data, "it has become clear that the spread of coronavirus will be far wider than assumed in our baseline forecast, pointing to a deeper – and possibly more prolonged – slowdown."[2]

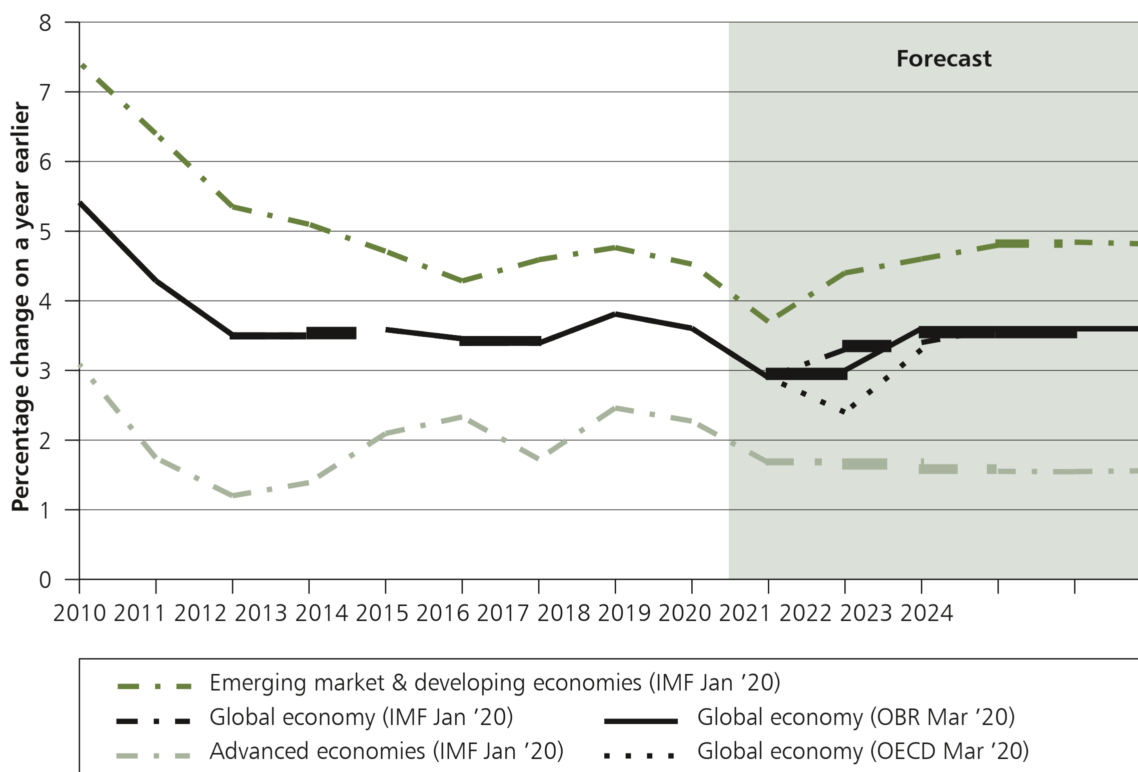
**1.9** There have already been clear signs that activity in China, where the outbreak began, has slowed. In its most recent economic assessment published on 2 March 2020, the Organisation for Economic Co-operation and Development (OECD) downgraded its forecast for Chinese growth in 2020 by 0.8 percentage points, to 4.9%.

**1.10** Highly integrated just-in-time manufacturing processes across the globe mean that disruption to Chinese output is likely to affect production globally. Lower Chinese growth will affect global demand. There will also be spillovers through financial markets and potential hits to business and consumer confidence.

**1.11** The OECD has produced two scenarios. In the 'baseline' scenario it assumes the virus is contained largely in China and revised down expectations of global growth in 2020 from 2.9% to 2.4%. In a second scenario, assuming broader contagion, the OECD suggests that global growth could be reduced more significantly in 2020, to 1.5%.

[2] 'Economic and fiscal outlook', OBR, March 2020.

**Chart 1.1: Global GDP growth**




*Source: International Monetary Fund; Office for Budget Responsibility; OECD, baseline scenario.*

## UK economy

**1.12** The OBR closed its forecast before the spread of COVID-19 in the UK, noting that this means "the precise forecasts for the economy … can no longer be regarded as central."[3] As an open economy, the UK will be affected because of the wider impacts the outbreak is having on the global economy. The OBR's estimate of the impact on global growth, based on the spread of the virus being relatively limited, reduces UK GDP growth by 0.1 percentage points this year.

**1.13** The impact of a wider spread outbreak of COVID-19 on the UK economy is highly uncertain. The drivers of any economic impact are health-related factors, including how many people get infected, the persistence of an outbreak and measures put in place to protect public health and prevent the spread. There will likely be significant, temporary disruption to the economy. Disruption could include temporary absences from work and interruptions to global supply chains, both of which would constrain the UK's productive capacity for a temporary period. In addition, the economy could be affected by a reduction in consumer spending and lower business investment, largely reflecting the response to measures to contain the outbreak, and weaker demand for UK exports.

### Growth

**1.14** The Office for National Statistics (ONS) estimates that the UK economy grew by 1.4% in 2019, 0.1 percentage points higher than in 2018. Delays to the UK's departure from the EU affected the profile of economic activity throughout 2019, leading to volatility in quarterly growth over the year.

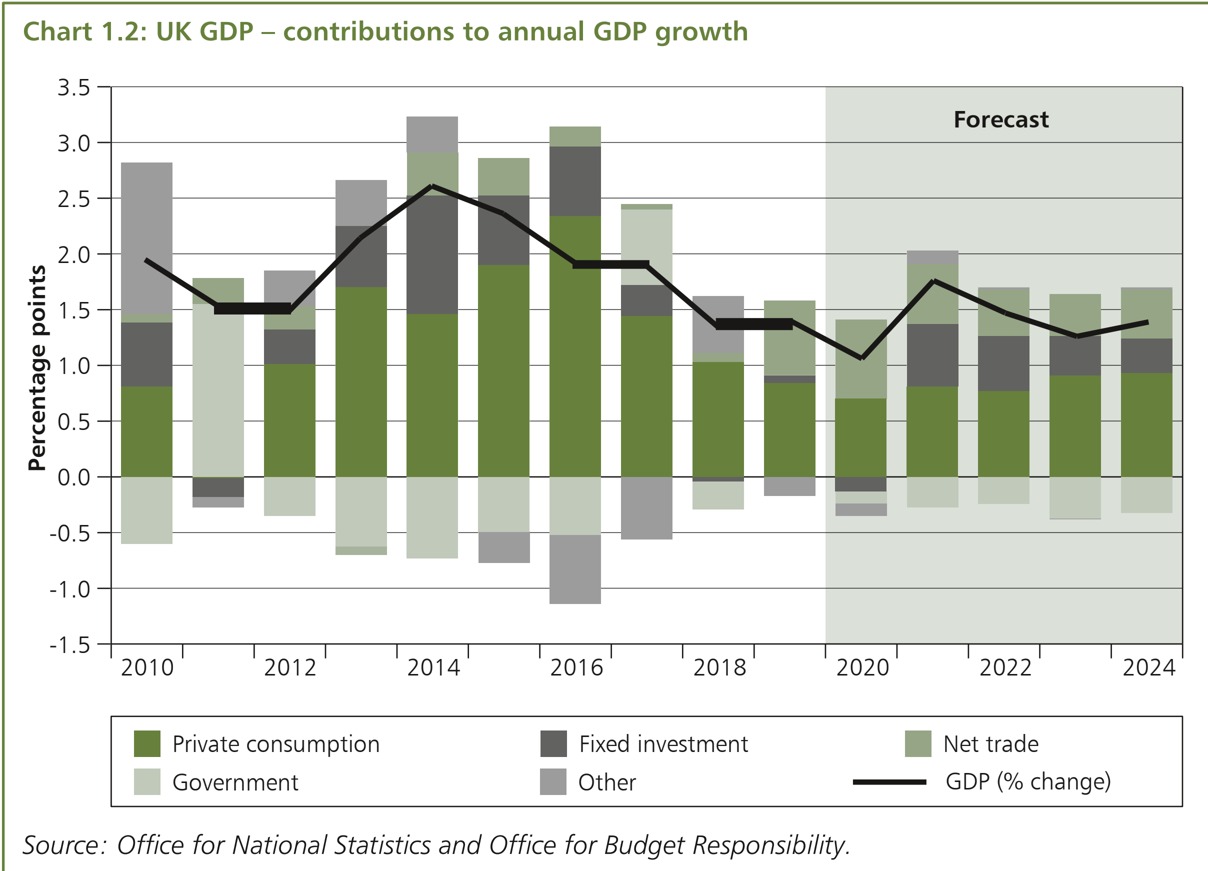
**1.15** Growth is distributed unevenly across the UK. England has historically had the highest GDP growth, averaging 2.2% between 1998 and 2018. Over the same period, Wales grew at an average rate of 1.7%, while Scotland and Northern Ireland both grew at an average rate

[3] 'Economic and fiscal outlook', OBR, March 2020.

of 1.9%. Growth is also uneven at a regional level – London has seen the fastest growth of all regions, averaging 3.1% between 1998 and 2018, while the North East of England had an average growth rate of 1.5%, the slowest of all regions.

**1.16** Over the forecast, the OBR has revised down its forecast for cumulative GDP growth by 0.5 percentage points, largely reflecting downward revisions to potential productivity and net migration. The OBR expects GDP growth of 1.1% in 2020, revised down from 1.4% in its Spring Statement 2019 forecast, with weaker contributions from both consumption and business investment growth. The OBR expects annual consumption growth to be 1.1% and for there to be no growth in business investment in 2020 (Chart 1.2). GDP growth is then expected to increase to 1.8% in 2021 before slowing slightly, reaching 1.4% in 2024.

**Chart 1.2: UK GDP – contributions to annual GDP growth**




*Source: Office for National Statistics and Office for Budget Responsibility.*

## The labour market and earnings

**1.17** Employment is at a record high. The number of people aged 16 years and over in paid work was 32.8 million in 2019 and was at a record high of 32.9 million in the three months to December 2019. The employment rate – the proportion of people aged 16 to 64 who are in paid work – also reached a record high of 76.5% in the same period (Chart 1.3). The OBR expects the employment level to increase further over the forecast period, reaching 33.4 million in 2024.

**Chart 1.3: UK employment and unemployment rates since 1971[1,2]**

[1] Employed people as a percentage of the population (aged 16-64).
[2] Unemployed people as a percentage of the economically active population (aged 16+).

*Source: Office for National Statistics.*

**1.18** The unemployment rate – the proportion of the economically active population (those in work plus those seeking and available to work) who are unemployed – was 3.8% in the three months to December 2019, the joint-lowest in over 40 years. The OBR expects the annual unemployment rate to remain at 3.8% in 2020 and 2021, before rising to 4.1% by 2024.

**1.19** Every nation and region of the UK has higher employment and lower unemployment than in 2010. Wales has seen the largest reduction in its unemployment rate since 2010, of 5.6 percentage points. There are 3.9 million more people in work than in 2010, with over 60% of the increase taking place in UK nations and regions outside London and the South East. Table 1.1 gives national and regional labour market statistics for the three months to December 2019.

**1.20** Earnings growth remains above inflation. Nominal wage growth (including bonuses) and regular nominal wage growth (excluding bonuses) were 2.9% and 3.2% respectively in the final quarter of 2019. Over the same period, real total pay growth was 1.4% and real regular pay growth was 1.8%. The OBR forecasts average earnings to grow by 3.3% in 2020 and rise to 3.6% in 2021.[4] It then expects growth to fall back to 3.1% by 2024.

**1.21** Rising real wages have helped to support the growth of real household disposable income (RHDI) per head, a measure of living standards. RHDI per head grew by 0.3% in the year to Q3 2019, down from 1.0% in the year to Q2 2019. The OBR expects annual growth in RHDI per head of 0.6% in 2020, before reaching 1.1% by 2024.[5]

[4] The OBR uses wages and salaries divided by employees to estimate wage growth, and so this will not necessarily correspond to the ONS headline Average Weekly Earnings measure.
[5] The OBR's measure of RHDI per head differs from the ONS's by including households and non-profit institutions serving households (NPISH) in the calculations, whereas the ONS measure refers to households only.

**Table 1.1: National and regional employment and unemployment rates (3 months to December 2019)**

| | Employment rate | | Unemployment rate | |
|---|---|---|---|---|
| | Actual[1] | Difference from UK average[3] | Actual[2] | Difference from UK average[3] |
| North East | 71.1 | -5.4 | 6.1 | 2.3 |
| North West | 75.9 | -0.6 | 4.2 | 0.4 |
| Yorkshire & the Humber | 73.3 | -3.2 | 4.5 | 0.7 |
| East Midlands | 78.4 | 1.9 | 3.6 | -0.2 |
| West Midlands | 75.5 | -1.0 | 4.4 | 0.6 |
| East of England | 78.6 | 2.1 | 3.3 | -0.5 |
| London | 75.5 | -1.0 | 4.3 | 0.5 |
| South East | 80.0 | 3.5 | 3.1 | -0.7 |
| South West | 80.1 | 3.6 | 2.8 | -1.0 |
| Wales | 74.4 | -2.1 | 2.9 | -0.9 |
| Scotland | 75.0 | -1.5 | 3.5 | -0.3 |
| Northern Ireland | 72.4 | -4.1 | 2.4 | -1.4 |
| **United Kingdom** | **76.5** | **0.0** | **3.8** | **0.0** |

[1] Employed people as a percentage of the population (aged 16-64).

[2] Unemployed people as a percentage of the economically active population (aged 16+).

[3] Percentage points.

*Source: Office for National Statistics.*

## Productivity

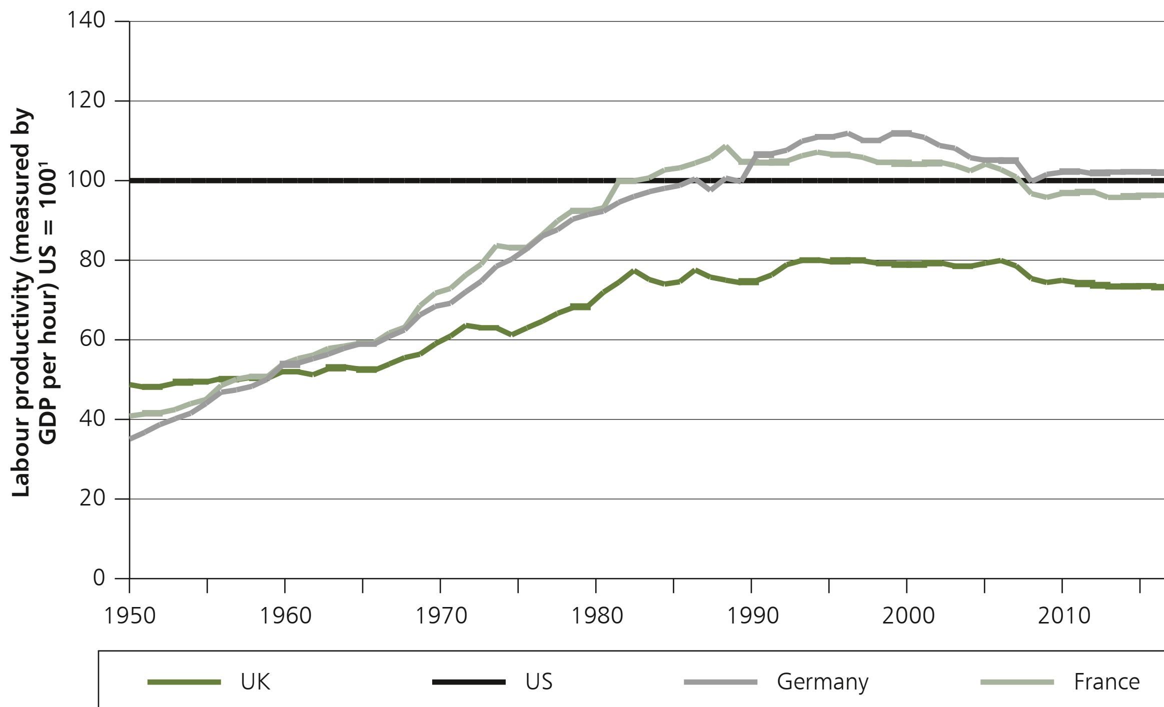
**1.22** UK labour productivity (measured as output per hour) did not grow at all in 2019, following subdued growth of 0.5% in 2018. This weakness has partly contributed to the OBR's judgement to revise down potential productivity growth – the underlying rate that determines how quickly productivity can grow sustainably – by an average of 0.1 percentage points per year across the forecast.[6] The OBR does note that "the significant planned increase in public investment potentially boosts productivity by raising the public capital stock, but we have assumed that the effect is likely to be felt mainly beyond our forecast horizon."[7]

**1.23** The UK's level of productivity has been lower than that of other advanced economies since the 1960s. The UK's level of productivity is more than 20% lower than other major advanced economies such as the US, France and Germany (Chart 1.4). In addition, UK productivity growth has slowed more since the financial crisis than other advanced economies. UK productivity growth has averaged 0.3% since 2008, slowing from 2.3% in the decade prior. By comparison, growth across the G7 has averaged 0.8% since 2008, compared to 1.9% in the decade prior.

[6] The OBR's productivity growth forecast is based on Non-North Sea Gross Value Added (GVA) per hour, which is different from the ONS productivity growth measure.

[7] 'Economic and fiscal outlook', OBR, March 2020.

**Chart 1.4: Comparison of productivity levels relative to US**



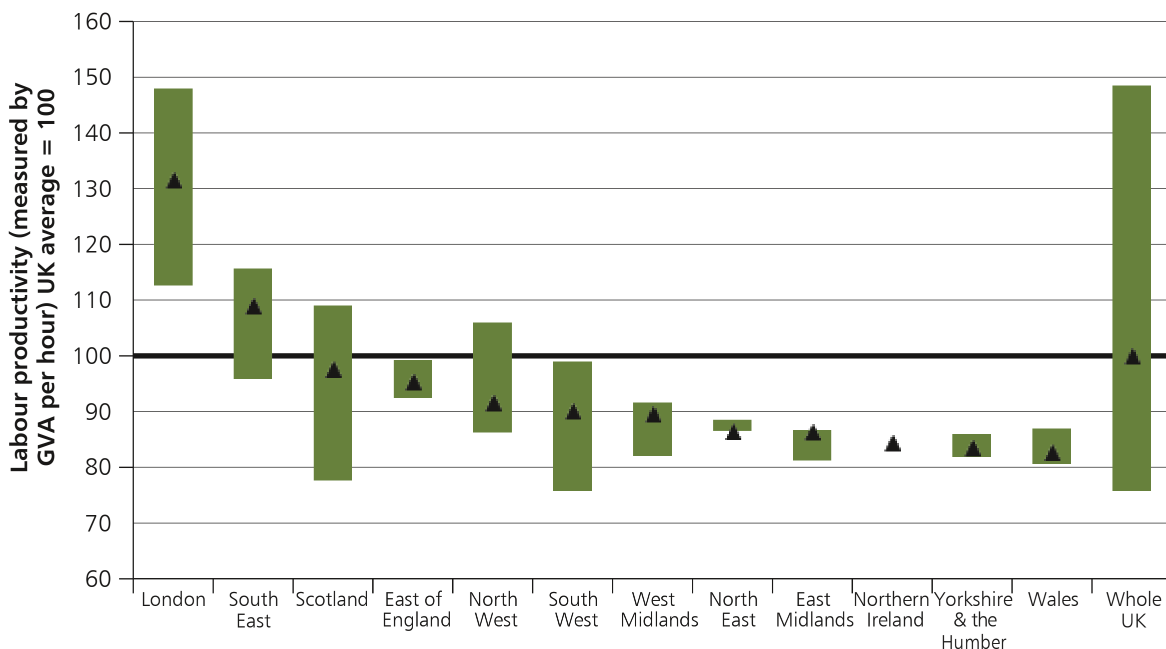

[1] 2010 US$ on a Purchasing Power Parity basis.

*Source: Data drawn from Bergeaud, Cette and Lecat (2016).*

**1.24** There is wide variation in productivity within the UK. As measured by output per hour, the only two areas with average levels of productivity above the UK average in 2018 were London (31.6% higher than the UK average) and the South East (9.1% higher than average). Productivity can vary significantly within each of the nations and regions as well as between them (Chart 1.5).

**1.25** In the long term, higher productivity remains the only path to sustainable economic growth and rising living standards. Investing in skills and infrastructure to improve productivity across the UK permits growth by enabling firms to pay higher wages, offer goods and services at lower prices, and increase their profits. Productivity improvements, by enhancing economic growth, are also a fundamental source of long-run growth in tax receipts and the government's ability to fund public services. A low average level of productivity – as well as significant variation between and within regions – are signs of untapped economic potential. The government is committed to levelling up investment across nations and regions to improve living standards nationally, as well as to address disparities in economic and social outcomes.

**Chart 1.5: Spread of productivity across the UK, 2018[1,2,3,4]**




[1] Estimates are provided for Gross Value Added (GVA) of all NUTS1 areas in the UK – defined as major socio-economic regions that typically have populations of 3 to 7 million. (NUTS = Nomenclature of Territorial Units for Statistics).
[2] The ranges show the minimum and the maximum level of nominal productivity within each NUTS1 region, using estimates of the productivity of NUTS2 areas within them. NUTS2 areas are smaller and typically have populations of 0.8 to 3 million.
[3] Triangles represent the average productivity for each NUTS1 region.
[4] The ONS do not publish GVA per hour for subregional breakdowns in Northern Ireland.

*Source: Office for National Statistics.*

## Prices

**1.26** The annual rate of Consumer Prices Index (CPI) inflation was 1.8% in 2019, down from 2.5% in 2018. Inflation fell through much of 2019, reaching 1.4% in the final quarter of the year, before increasing to 1.8% in January 2020. The ONS's headline measure of inflation, the Consumer Prices Index including owner occupiers' housing costs (CPIH), was also 1.8% in January 2020.[8] The OBR forecasts CPI inflation to be 1.4% in 2020, gradually rising to 2.1% in 2022 and 2023, and settling at 2.0% by 2024.

**1.27** Alongside the Budget, the government and UK Statistics Authority (UKSA) are launching a consultation, announced on 4 September 2019,[9] on UKSA's proposal to address the shortcomings of the Retail Prices Index (RPI) measure of inflation. The consultation will cover, among other things, the issue of timing, including whether the UKSA's proposal might be implemented at a date other than 2030, and if so, when between 2025 and 2030, and issues on technical matters concerning the implementation of its proposal. The consultation will be open for a period of six weeks, closing on 22 April 2020. The government and UKSA will respond to the consultation before the Parliamentary summer recess.

## Current Account

**1.28** The current account measures the flow of goods, services, income and transfers between the UK and the rest of the world. In 2018, the current account balance widened to a deficit of 3.9% of GDP from 3.5% in 2017. This was driven by a widening of both the trade and income deficits. The current account deficit averaged 4.7% of GDP in the first three quarters of 2019. The OBR expects the current account deficit for the whole of 2020 to be 3.8%. It is then forecast to remain close to 4.0% of GDP throughout the forecast period.

[8] CPIH extends CPI to include costs associated with owning, maintaining and living in one's own home as well as council tax.
[9] 'Letter from the Chancellor of the Exchequer', HM Treasury, September 2019.

## Monetary Policy

**1.29** The Monetary Policy Committee (MPC) of the Bank of England has operational independence to set monetary policy to meet its primary objective of price stability and, subject to that, to support the economic policy of the government, including its objectives for growth and employment.

**1.30** Independent monetary policy is a critical element of the UK's macroeconomic framework, alongside sustainable public finances and a resilient financial system. Low and stable inflation supports living standards and provides certainty for households and businesses, helping them make decisions about saving, investment and spending.

**1.31** The Chancellor is responsible for setting the MPC's remit. In the Budget, the Chancellor reaffirms the symmetric inflation target of 2% for the 12-month increase in the CPI measure of inflation. This target applies at all times.[10] The Chancellor also confirms that the Asset Purchase Facility (APF) will remain in place for the financial year 2020-21.

**Table 1.2: Summary of the OBR's central economic forecast (percentage change on year earlier, unless otherwise stated)[1]**

| | | Forecast | | | | |
|---|---|---|---|---|---|---|
| | **2019** | **2020** | **2021** | **2022** | **2023** | **2024** |
| **GDP growth** | **1.4** | **1.1** | **1.8** | **1.5** | **1.3** | **1.4** |
| **GDP growth per capita** | **0.8** | **0.5** | **1.3** | **1.1** | **0.9** | **1.1** |
| **Main components of GDP** | | | | | | |
| Household consumption[2] | 1.3 | 1.1 | 1.2 | 1.2 | 1.4 | 1.4 |
| General government consumption | 3.6 | 3.7 | 2.8 | 2.1 | 1.9 | 2.2 |
| Fixed investment | 0.4 | -0.8 | 3.4 | 2.9 | 2.0 | 1.8 |
| Business investment | 0.3 | 0.0 | 1.8 | 3.0 | 2.4 | 2.3 |
| General government | 2.1 | 1.9 | 10.9 | 4.6 | 1.8 | 1.2 |
| Private dwellings[3] | -0.3 | -4.2 | 1.5 | 1.6 | 1.3 | 1.2 |
| Change in inventories[4] | 0.1 | -0.1 | 0.1 | 0.0 | 0.0 | 0.0 |
| Net trade[4] | 0.0 | -0.1 | -0.3 | -0.2 | -0.4 | -0.3 |
| **CPI inflation** | **1.8** | **1.4** | **1.8** | **2.1** | **2.1** | **2.0** |
| **Employment (millions)** | **32.8** | **33.0** | **33.1** | **33.2** | **33.3** | **33.4** |
| **Unemployment (% rate)** | **3.8** | **3.8** | **3.8** | **3.9** | **4.0** | **4.1** |
| **Productivity per hour** | **0.0** | **0.9** | **1.2** | **1.2** | **1.1** | **1.2** |

[1] All figures in this table are rounded to the nearest decimal place. This is not intended to convey a degree of unwarranted accuracy. Components may not sum to total due to rounding and the statistical discrepancy.

[2] Includes households and non-profit institutions serving households.

[3] Includes transfer costs of non-produced assets.

[4] Contribution to GDP growth, percentage points.

*Source: Office for National Statistics and Office for Budget Responsibility.*

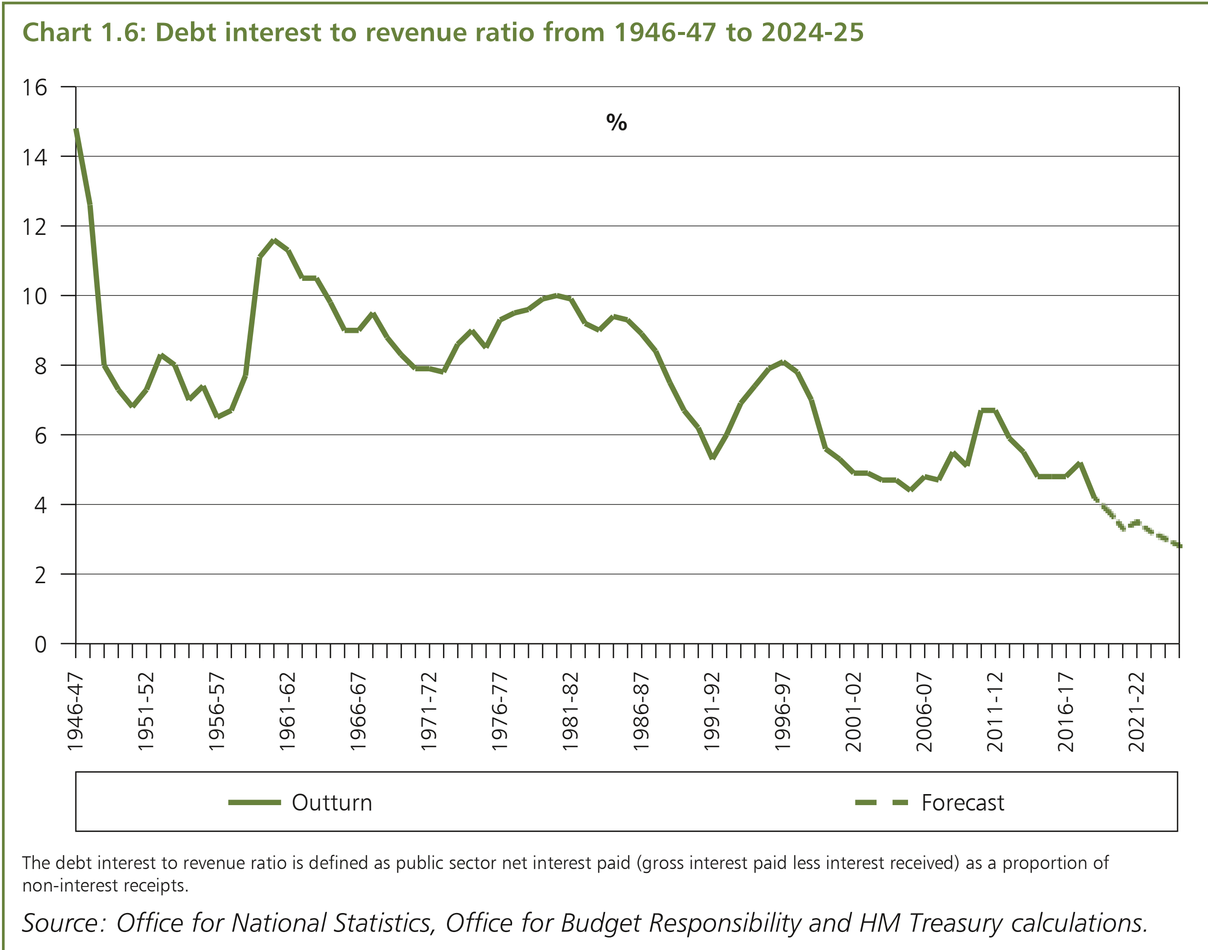
[10] 'Monetary policy remit: Budget 2020', HM Treasury, March 2020.

## Public finances

**1.32** Since 2010, the government has restored the public finances to health after inheriting a deficit at a post-war high and debt that had nearly doubled in two years. The deficit has been reduced by four-fifths from a peak of 10.2% of GDP in 2009-10 to 1.8% of GDP in 2018-19.[11] As Chart 1.6 and 1.7 show the cost of government debt as a share of government revenues is now at a post-war low, due to historically low interest rates on government borrowing.

**1.33** With low borrowing costs and the public finances in a more secure position, the government can support the economy and fund the response to COVID-19 in the short-term and take action over the medium-term to drive growth and improve public services, without compromising fiscal sustainability. In addition to short-term support for the COVID-19 response, the Budget provides for a significant medium-term increase in day-to-day spending on public services. With historically low borrowing costs, it is right that the government borrows to invest in the country's future and address challenges. The government is therefore borrowing to fund a new set of growth-enhancing policies focused on delivering a step-change in infrastructure investment, which aims to raise the UK's productivity growth in the long-run.

**Chart 1.6: Debt interest to revenue ratio from 1946-47 to 2024-25**

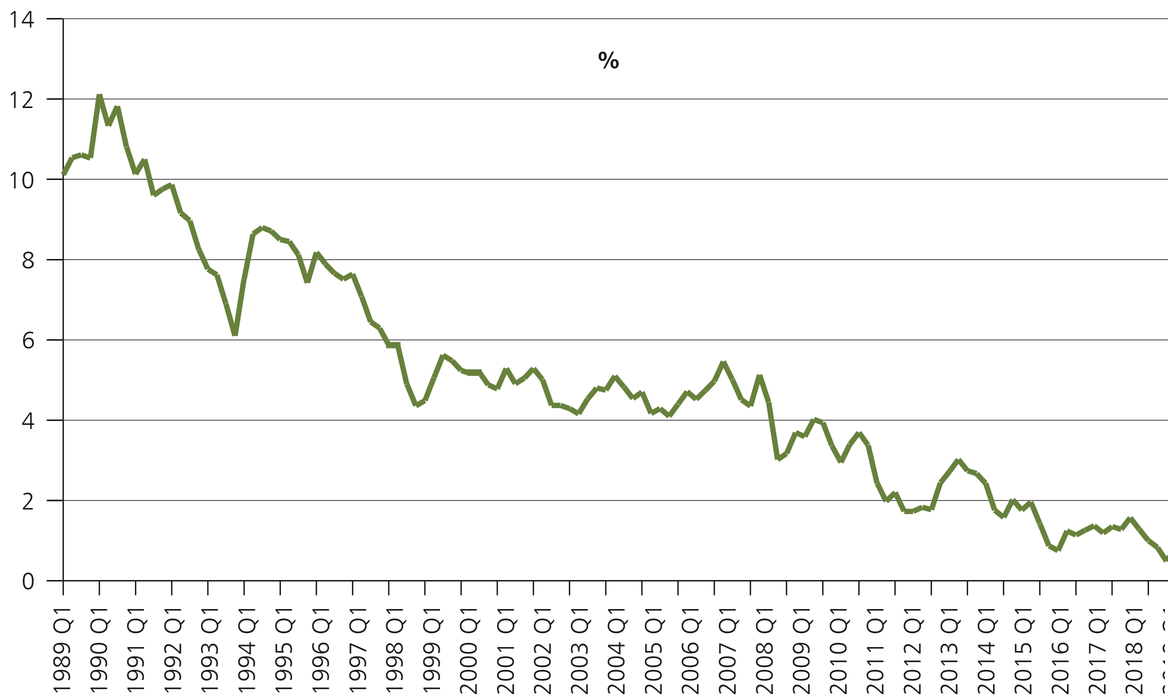



The debt interest to revenue ratio is defined as public sector net interest paid (gross interest paid less interest received) as a proportion of non-interest receipts.

*Source: Office for National Statistics, Office for Budget Responsibility and HM Treasury calculations.*

[11] Public Sector Finances, UK: January 2020; Office for National Statistics; February 2020.

**Chart 1.7: Historical quarterly 10-year gilt yields from 1989 to 2019**




Benchmark 10-year Treasury gilt yield from 1989 to year end 2019.

*Source: Bloomberg.*

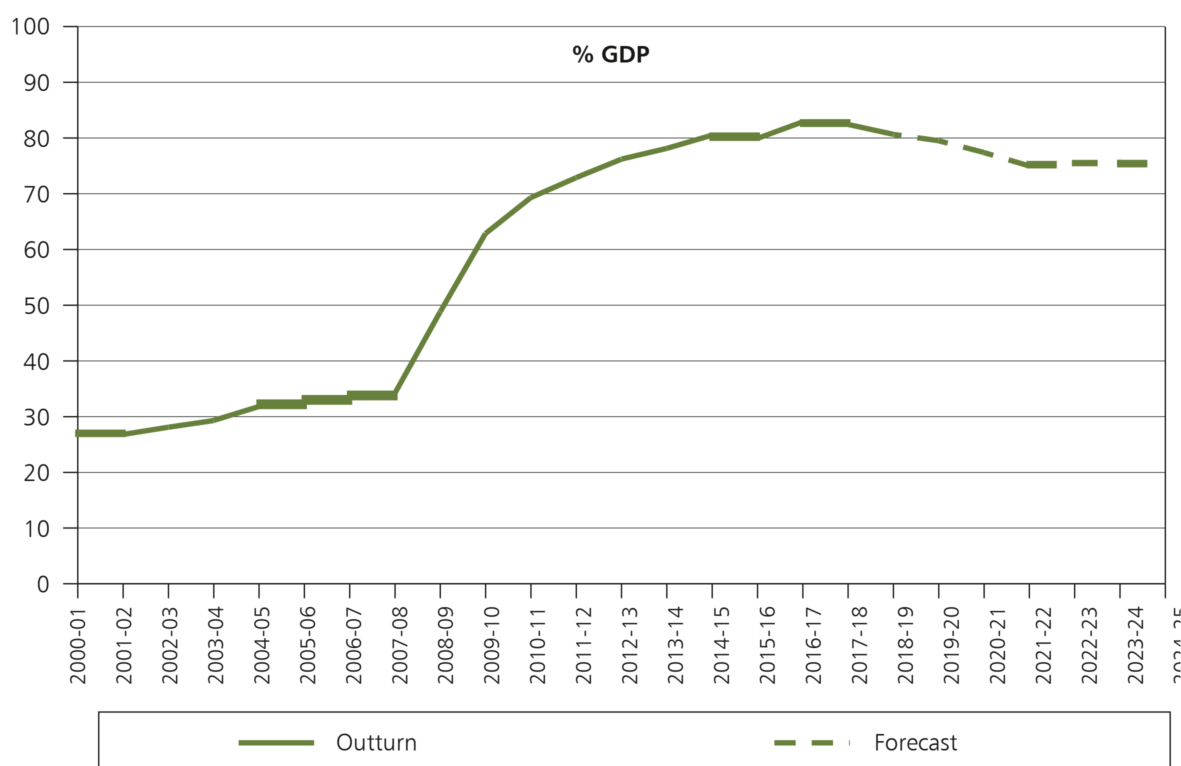
## The fiscal framework

**1.34** This Budget has been delivered to meet the following fiscal rules:

- to have the current budget at least in balance by the third year of the rolling five-year forecast period
- to ensure that public sector net investment (PSNI) does not exceed 3% of GDP on average over the rolling five-year forecast period
- if the debt interest to revenue ratio is forecast to remain over 6% for a sustained period, the government will take action to ensure the debt-to-GDP ratio is falling

**1.35** The Budget also sets the spending envelope for the upcoming CSR within these rules, which allow for significant investment in growth-enhancing infrastructure while maintaining control of day-to-day spending. They allow policy to meet the economic demands of today while ensuring that borrowing and debt remain under control. Chart 1.8 shows that public sector net debt has stabilised after the sharp rise driven by the financial crisis and is expected to be broadly stable across the forecast period. The rules also provide the flexibility to respond fully to near-term shocks to the economy and public finances such as from COVID-19.

**Chart 1.8: Public sector net debt from 2000-01 to 2024-25**




*Source: Office for National Statistics and Office for Budget Responsibility.*

**1.36** Interest rates are expected to remain at very low levels for an extended period. This has prompted an international debate around the implications of this environment for fiscal sustainability and the role of fiscal policy. In this context, the Chancellor has announced that HM Treasury will conduct a review of the UK's fiscal framework, to:

- ensure that it remains appropriate for the current macroeconomic environment
- support the ambitious new policy agenda of the government to invest in and level up every part of the country
- keep the United Kingdom at the leading edge of international best practice in macroeconomic policy

**1.37** The review will report back by Autumn Budget 2020, to allow the government to confirm its fiscal objectives for the Parliament. It will be undertaken by HM Treasury and will involve broad consultation with external experts from across the UK and internationally. The review will be guided by the following principles:

- fiscal policy should support the government's economic objectives, while maintaining the sustainability of the public finances by keeping control over borrowing and debt
- low and stable inflation should be supported, as an essential pre-requisite to deliver the government's economic objectives
- the UK's existing institutional strengths in fiscal policy making – the independent Office for National Statistics (ONS) producing official economic and fiscal statistics, and the independent OBR producing the official economic and fiscal forecasts and assessing the government's performance against its fiscal objectives – should be preserved and built on

**1.38** The review will consider the following areas:

- **The low interest rate environment:** It has been argued that, given persistently very low interest rates, there is further fiscal space to borrow for investment. This needs to be weighed against the risks posed by high levels of public debt, for example from rapid changes in economic conditions and from longer-term fiscal pressures. The review will look at how to balance the opportunities and risks within the fiscal framework.

- **Macroeconomic stabilisation:** The review will consider the case for a more active role for fiscal policy in stabilising the economy, especially if there is reduced space for monetary policy due to low interest rates. This will be judged alongside consideration of the extent to which active fiscal policy can provide timely and effective demand management, and the implications for wider policy objectives and fiscal sustainability. The review will look at how to reflect these trade-offs within the fiscal framework.

- **Incentives for value for money prioritisation:** The fiscal framework should support the prioritisation of public investments which most enhance growth. The review will consider whether some well-evidenced spending, beyond what the current international frameworks class as capital investment, is currently disincentivised. This will include an assessment of the practical challenges in evolving the framework: including measurement issues, consistency with internationally recognised statistical and accounting frameworks, how other countries have approached these issues, and the need to balance fiscal sustainability objectives.

- **Developments in the management and measurement of the balance sheet:** Completion of HM Treasury's Balance Sheet Review discussed in Box 1.A in the summer provides an opportunity to consider its conclusions and options to improve the management of loans, guarantees, contingent liabilities, and wider balance sheet transactions. The review will also consider the strengths and limitations of using broader balance sheet measures to assess fiscal sustainability.

- **Mitigating fiscal risks and pressures:** The review will consider how to further support the effective management of fiscal pressures and risks, through a framework which can provide operationally-effective controls on the short and medium-term fiscal position, and can address and mitigate the challenge of longer-run pressures on fiscal sustainability, including from the ageing population and the actions needed to achieve net zero by 2050.

- **Building on the strength of the UK's world class institutions:** The review will consider options to support and strengthen the practices and institutions that deliver the UK's fiscal framework, including the independent OBR and ONS, and advisory bodies such as the National Infrastructure Commission. The review will also consider the case for strengthening the legislative underpinning for the UK's system of public financial management.

**1.39** When the review is concluded, HM Treasury will lay before Parliament a new Charter for Budget Responsibility; the Autumn 2016 Charter therefore remains in force at the current time.[12] The Budget has been delivered within the fiscal rules set out above in paragraph 1.34. The Chancellor wrote to the OBR ahead of the Budget to ask it to assess the government against these rules, in addition to those set out in the Autumn 2016 Charter.[13]

[12] Charter for Budget Responsibility: autumn 2016 update; HM Treasury, January 2017.

[13] ibid.

**Box 1.A: Balance Sheet Review**

The government manages assets worth £2 trillion alongside £4.6 trillion of liabilities on behalf of citizens.[14] The Balance Sheet Review (BSR) was launched in 2017 to identify opportunities to dispose of assets that no longer serve a policy purpose, improve returns on retained assets, and reduce the risk and cost of liabilities. This work aims to put the UK at the forefront of the international drive to reduce waste and deliver improvements in the cost-effective management of public wealth, as recognised by the IMF in its October 2018 Fiscal Monitor. The BSR will conclude and report at this year's Comprehensive Spending Review.

***Strengthening the assessment of balance sheet transactions***

The BSR has highlighted the importance of considering the impacts on the government's balance sheet, as well as on income flows over the longer term, when deciding to buy or sell assets and settle or incur liabilities. The government is therefore considering a new framework to evaluate the case for proceeding with significant balance sheet transactions. This will take into account impacts across a range of fiscal metrics, including Public Sector Net Debt (PSND), Public Sector Net Financial Liabilities (PSNFL) and Public Sector Net Worth (PSNW). The government will work with the ONS and OBR to further develop statistics and forecasts for PSNW and depreciation in the public sector finances, as well as assessing how these reconcile with the Whole of Government Accounts (WGA). This will inform the fiscal framework review set out in paragraphs 1.36 to 1.39.

***Managing risk from contingent liabilities***

The government is exposed to £192 billion of contingent liabilities, including guarantees and insurance provided to the private sector.[15] The BSR has developed proposals to improve the management of these liabilities and address a key balance sheet risk recognised by the OBR in its July 2019 Fiscal Risk Report.[16] The government is publishing a report alongside Budget: 'Government as insurer of last resort' providing more detail on the policy approach.

***Knowledge assets***

To improve social, economic and financial returns from its c.£150 billion[17] of knowledge assets in the public sector, and following publication of a report at Budget 2018,[18] the government will establish a new unit and fund to develop knowledge assets.

## The fiscal outlook

**1.40** Borrowing this year is forecast to be £47.4 billion, £0.2 billion lower than the OBR's restated March 2019 forecast. Underlying receipts are forecast to be £4.9 billion higher, driven by a combination of stronger National Insurance contributions (NICs), capital gains tax and onshore corporation tax receipts. The strength in receipts is offset by higher spending, which is forecast to be £5.3 billion higher and is largely due to an increase in local and public corporations' capital expenditure, an increase in company tax credits and lower than expected underspends by government departments. Policy decisions made by the government at Spending Round 2019 and at Budget, and described in Chapter 2, decrease borrowing by £0.6 billion in 2019-20.[19]

[14] 'Whole of Government Accounts 2017 to 2018'; HM Treasury; May 2018.
[15] ibid.
[16] 'Fiscal Risks Report 2019'; Office for Budget Responsibility; July 2019.
[17] 'Measuring Intangible Capital in the Public Sector'; SPINTAN; December 2016.
[18] Getting smart about intellectual propery and other intangibles in the public sector: Budget 2018; HM Treasury; October 2018
[19] 'Economic and fiscal outlook', OBR, March 2020.

**1.41** Across the rest of the forecast, compared to the OBR's restated March 2019 forecast, the underlying forecast for borrowing is expected to be higher by £3.1 billion on average from 2020-21 onwards. The changes in the underlying fiscal outlook are due to a combination of the following factors:

- A downward revision to underlying receipts from 2020-21 onwards that is predominantly driven by downward revisions to growth in GDP and its components. Excluding a fiscally neutral switch that means that customs duty revenues previously remitted to the EU are now recognised in both receipts and spending, receipts are lower by an average of £3.0 billion a year from 2020-21 onwards. Lower wage growth, consumer spending and profits, and an adjustment to fuel efficiency assumptions have downward effects on income tax and NICs, VAT, corporation tax and fuel duty receipts respectively. Lower interest rates reduce the interest received from government assets.
- Underlying spending (excluding debt interest expenditure) is forecast to be higher in every year from 2020-21 onwards. Excluding the fiscally neutral change to the treatment of customs duties, non-interest spending is higher by an average of £7.4 billion. Higher expenditure on welfare, company tax credits, capital transfers associated with new student loans, and capital spending by local government are the main reasons for this increase.
- However, underlying debt interest expenditure has been revised down by £7.4 billion on average from 2020-21 onwards. This is due to downward revisions in the forecasts for RPI inflation and interest rates.

**1.42** The most significant changes to the forecast since restated March 2019 are the decisions taken by the government in the Budget and described in Chapter 2, which increase borrowing across the forecast. On average they increase borrowing by £21 billion from 2020-21 onwards. The direct cost of the measures is partly offset by the positive short-term impact on the fiscal position of the higher economic growth that is generated as a result of the Budget package. Higher growth in the short term, and a medium-term increase in nominal GDP leads to increased tax revenues. This is partly offset by the effect of higher borrowing, interest rates and inflation which increase debt interest and welfare spending.

**1.43** In the usual way, the OBR have incorporated Budget policy decisions (set out in Table 2.1) into their final post-measures forecast. The government has not asked the OBR to incorporate the fiscal and economic impacts of the government's plan to tackle the economic impact of COVID-19 into their final forecast. This reflects that the OBR's baseline forecast does not incorporate the most recent estimate of the likely economic and fiscal impacts of a spread of COVID-19 and to do so would have introduced an inconsistency between the baseline forecast and the policy package. Moreover, given the fast-developing situation, the government will continue to adapt its policy to best respond to the latest circumstances. The OBR has said that, relative to their Budget forecast, COVID-19 is likely to put upward pressure on borrowing in the short term but expect limited impact over the medium and longer term.

**1.44** The government will therefore reflect the costs of its response to COVID-19 at a future fiscal event alongside an updated OBR forecast. The current fiscal framework provides the near-term flexibility to respond fully to the challenge of COVID-19, and the government has built headroom against the medium-term rules should it be needed.

### Table 1.3: Changes to the OBR's forecast for public sector net borrowing since restated March 2019 forecast (£ billion)

| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|
| **Restated March 2019** | **47.6** | **40.2** | **37.6** | **35.4** | **33.3** |
| Total underlying forecast changes since restated March 2019[1] | 0.4 | 2.3 | 5.1 | 3.6 | 1.5 |
| *of which* | | | | | |
| Receipts forecast[2] | -4.9 | 1.0 | 3.5 | 4.1 | 3.5 |
| Debt interest forecast | -2.0 | -6.7 | -6.6 | -7.7 | -8.5 |
| Other spending forecast[2] | 7.3 | 7.9 | 8.2 | 7.1 | 6.5 |
| Total effect of government decisions since March 2019[1] | -0.6 | 12.3 | 24.0 | 22.5 | 25.4 |
| *of which* | | | | | |
| Direct effects | -0.6 | 15.6 | 31.1 | 32.2 | 33.8 |
| Indirect effects | 0.0 | -3.3 | -7.1 | -9.7 | -8.4 |
| **Total changes since restated March 2019** | **-0.2** | **14.6** | **29.1** | **26.0** | **26.9** |
| **Budget 2020** | **47.4** | **54.8** | **66.7** | **61.5** | **60.2** |

Figures may not sum due to rounding.

[1] Equivalent to lines from Table 1.3 of the OBR (March 2020) 'Economic and fiscal outlook'; full references available in 'Budget 2020 data sources'.

[2] Excludes a fiscally neutral change to the treatment of customs duty revenues previously remitted to the EU.

*Source: Office for Budget Responsibility and HM Treasury calculations.*

**1.45** Compared to the restated March 2019 forecast, borrowing is lower in 2019-20, but higher in every other year of the forecast. It rises over the forecast period from 2.1% of GDP in 2019-20 to 2.8% of GDP in 2021-22, before falling to 2.2% in 2024-25.

### Table 1.4: Overview of the OBR's borrowing forecast as a percentage of GDP

| | Outturn | Forecast | | | | | |
|---|---|---|---|---|---|---|---|
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Public sector net borrowing | 1.8 | 2.1 | 2.4 | 2.8 | 2.5 | 2.4 | 2.2 |
| Cyclically-adjusted public sector net borrowing | 1.9 | 2.2 | 2.4 | 3.0 | 2.7 | 2.5 | 2.2 |
| General government net borrowing[1] | 1.8 | 2.2 | 2.5 | 3.1 | 2.6 | 2.4 | 2.4 |
| *Memo: Output gap[2]* | *0.3* | *0.0* | *0.1* | *0.4* | *0.4* | *0.1* | *0.0* |

[1] Consistent with Manual on Government Deficit and Debt, Eurostat, 2019.

[2] Output gap measured as a percentage of potential GDP.

*Source: Office for National Statistics and Office for Budget Responsibility.*

**1.46** Compared with the restated March 2019 forecast, debt is lower in 2020-21, it is then higher in all the remaining years of the Budget forecast as a share of GDP, largely as a result of higher borrowing. Public sector net debt is expected to continue to fall over the forecast, from 79.5% in 2019-20, to a low of 75.0% in 2021-22 before rising slightly to 75.2% in 2024-25. Public sector net debt ex Bank of England is broadly stable across the forecast.

### Table 1.5: Overview of the OBR's debt forecast as a percentage of GDP

| | Outturn | Forecast | | | | | |
|---|---|---|---|---|---|---|---|
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Public sector net debt[1] | 80.6 | 79.5 | 77.4 | 75.0 | 75.4 | 75.6 | 75.2 |
| Public sector net debt ex Bank of England[1] | 72.3 | 71.9 | 71.9 | 72.3 | 72.9 | 73.1 | 72.9 |
| Public sector net financial liabilities[1] | 67.4 | 66.7 | 65.9 | 65.3 | 64.9 | 64.5 | 63.4 |
| General government gross debt[2] | 84.1 | 83.2 | 82.9 | 83.2 | 83.3 | 83.3 | 83.0 |

[1] Debt and liabilities at end of March; GDP centred on end of March.

[2] Consistent with Manual on Government Deficit and Debt, Eurostat, 2019.

*Source: Office for National Statistics and Office for Budget Responsibility.*

**Table 1.6: Changes to the OBR's forecast for public sector net debt since restated March 2019 forecast as a percentage of GDP**

| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
|---|---|---|---|---|---|
| **Restated March 2019** | **81.3** | **78.2** | **74.3** | **73.6** | **72.7** |
| Total forecast changes since restated March 2019[1] | -1.8 | -0.8 | 0.7 | 1.9 | 2.9 |
| *of which* | | | | | |
| Change in nominal GDP[2] | -1.0 | -1.1 | -1.2 | -1.0 | -0.9 |
| Change in cash level of net debt | -0.8 | 0.4 | 1.9 | 2.9 | 3.8 |
| **Budget 2020** | **79.5** | **77.4** | **75.0** | **75.4** | **75.6** |

Figures may not sum due to rounding.

[1] Equivalent to lines from Table 3.34 of the OBR (March 2020) 'Economic and fiscal outlook'; full references available in 'Budget 2020 data sources'.

[2] Non-seasonally adjusted GDP centred end of March.

*Source: Office for Budget Responsibility.*

**1.47** The OBR's 'Economic and Fiscal Outlook' shows that the government is forecast to meet the fiscal rules set out above in paragraph 1.34. There is a current budget surplus of £11.7 billion in 2022-23, providing headroom against this rule. Net investment is expected to average 2.9% of GDP over 2020-21 to 2024-25 – below the 3% target – while the debt interest to revenue ratio remains below 6%.

**Table 1.7: Metrics used for fiscal rules**

| | Forecast | | | | | |
|---|---|---|---|---|---|---|
| | **2019-20** | **2020-21** | **2021-22** | **2022-23** | **2023-24** | **2024-25** |
| Current budget deficit (% of GDP) | -0.1 | -0.2 | -0.1 | -0.5 | -0.7 | -0.8 |
| Public sector net investment (% of GDP) | 2.2 | 2.6 | 2.9 | 3.0 | 3.0 | 3.0 |
| Debt interest to revenue ratio[1] | 3.8 | 3.3 | 3.5 | 3.3 | 3.1 | 2.9 |

[1] The debt interest to revenue ratio is defined as public sector net interest paid (gross interest paid less interest received) as a proportion of non-interest receipts.

*Source: Office for Budget Responsibility.*

## Public spending

**1.48** The government's significant progress in restoring the public finances to health over the last decade means it can now afford to support the economy in the short term while investing to support long-term growth. The new fiscal framework allows for a significant increase in growth-enhancing infrastructure investment, while maintaining control of day-to-day spending and the commitment to long-term fiscal sustainability.

**1.49** At Spending Round 2019, the government increased departmental spending by 4.1% in real terms between 2019-20 and 2020-21, delivering the fastest planned growth in day-to-day departmental spending in 15 years.[20] Spending Round 2019 funded vital public services: high-quality, readily accessible healthcare; schools and colleges that ensure every child receives a superb education; and action to cut crime and help keep our streets safe.

**1.50** Individual budgets for all departments have been set until 2020-21 for both departmental capital totals (CDEL) and departmental resource totals (RDEL). Longer-term settlements have already been announced for the NHS and schools, which have confirmed budgets until 2023-24 and 2022-23 respectively.

[20] Spending Round 2019; HM Treasury; September 2019.

**Table 1.8: Departmental Capital Budgets in 2019-20 and 2020-21 (Capital DEL, in £ billion)**

| | 2019-20 | 2020-21 |
|---|---|---|
| **Capital DEL** | | |
| Health and Social Care | 7.1 | 8.2 |
| Education | 4.6 | 4.5 |
| Home Office | 0.7 | 0.8 |
| Justice | 0.5 | 0.7 |
| Law Officers' Departments | 0.0 | 0.0 |
| Defence | 10.5 | 10.6 |
| Single Intelligence Account | 0.6 | 0.8 |
| Foreign and Commonwealth Office | 0.1 | 0.1 |
| International Development[1] | 2.0 | 4.8 |
| MHCLG Housing and Communities[2] | 8.4 | 13.1 |
| MHCLG Local Government | 0.0 | 0.0 |
| Transport[3] | 14.6 | 17.6 |
| Business, Energy and Industrial Strategy[4] | 11.2 | 12.3 |
| Digital, Culture, Media and Sport | 0.6 | 0.6 |
| Environment, Food and Rural Affairs | 0.8 | 0.9 |
| International Trade | 0.0 | 0.0 |
| Work and Pensions | 0.1 | 0.2 |
| HM Revenue and Customs | 0.3 | 0.4 |
| HM Treasury | 0.1 | 0.0 |
| Cabinet Office | 0.1 | 0.1 |
| Scotland | 4.4 | 5.5 |
| Wales[5] | 2.3 | 2.4 |
| Northern Ireland[6] | 1.4 | 1.7 |
| Small and Independent Bodies | 0.4 | 0.5 |
| Reserves[7] | 0.0 | 3.4 |
| Adjustment for Budget Exchange[8] | 0.0 | -0.6 |
| **Total Capital DEL** | **71.1** | **88.5** |
| *Remove CDEL not in PSGI[9]* | *-11.2* | *-13.3* |
| *Allowance for shortfall[10]* | *0.0* | *-3.9* |
| **Public Sector Gross Investment in CDEL** | **59.9** | **71.2** |

[1] Figures for 2020-21 do not reflect all transfers which will be made from DfID to other government departments.

[2] MHCLG's CDEL budget in 2020-21 includes technical adjustments along with Budget announcements since Budget 2018.

[3] DfT's CDEL budget in 2020-21 includes a net reduction due to business rates retention pilots.

[4] BEIS and other government departments' CDEL budgets increased in 2020-21 to account for the reclassification of R&D in the National Accounts.

[5] This includes the 5% needs-based Barnett formula uplift.

[6] This includes the 2.5% VAT abatement.

[7] 2020-21 adjusted to account for a change in the accounting treatment of leases. This money will be allocated to departments through the Estimates process.

[8] Departmental budgets in 2020-21 include amounts carried forward from 2019-20 through Budget Exchange, which will be voted at Main Estimates. These increases will be offset at Supplementary Estimates in future years so are excluded from spending totals.

[9] Capital DEL that does not form part of public sector gross investment, including financial transactions in Capital DEL.

[10] The OBR's forecast of underspends in Capital DEL budgets.

### Table 1.9: Departmental Resource Budgets in 2019-20 and 2020-21 (Resource DEL excluding depreciation, in £ billion)

| | 2019-20 | 2020-21 |
|---|---|---|
| **Resource DEL excluding depreciation**[1] | | |
| Health and Social Care | 133.3 | 139.8 |
| *of which: NHS England* | *123.7* | *129.9* |
| Education | 63.8 | 67.8 |
| *of which: Schools* | *44.4* | *47.6* |
| Home Office | 11.5 | 13.0 |
| Justice | 7.8 | 8.3 |
| Law Officers' Departments | 0.6 | 0.7 |
| Defence | 29.5 | 30.8 |
| Single Intelligence Account | 2.4 | 2.1 |
| Foreign and Commonwealth Office[2] | 2.4 | 1.1 |
| International Development[2] | 8.0 | 9.6 |
| MHCLG Housing and Communities[3] | 2.6 | 1.7 |
| MHCLG Local Government[3] | 5.2 | 8.2 |
| Transport | 3.8 | 4.2 |
| Business, Energy and Industrial Strategy | 2.5 | 2.5 |
| Digital, Culture, Media and Sport | 1.6 | 1.7 |
| Environment, Food and Rural Affairs[4] | 2.1 | 3.9 |
| International Trade | 0.5 | 0.5 |
| Work and Pensions | 5.7 | 5.8 |
| HM Revenue and Customs | 4.0 | 3.9 |
| HM Treasury | 0.4 | 0.2 |
| Cabinet Office | 1.0 | 0.5 |
| Scotland[5] | 16.9 | 21.1 |
| Wales[5,6] | 12.1 | 12.8 |
| Northern Ireland[7] | 11.2 | 11.5 |
| Small and Independent Bodies | 1.5 | 2.2 |
| Reserves | 0.0 | 6.7 |
| Adjustment for Budget Exchange[8] | 0.0 | -0.1 |
| **Total Resource DEL excluding depreciation** | **330.4** | **360.6** |
| *OBR allowance for shortfall*[9] | *-0.5* | *-3.2* |
| **OBR resource DEL excluding depreciation forecast** | **329.9** | **357.3** |

[1] Resource DEL excluding depreciation is the Treasury's primary control total within resource budgets and the basis on which Spending Round settlements were made.

[2] Figures for 2020-21 do not reflect all transfers which will be made from DfID to FCO and other government departments.

[3] MHCLG Housing and Communities DEL in 2020-21 excludes the New Homes Bonus, reflecting a transfer to Local Government (LG) DEL. LG DEL increase in 2020/21 is also driven by the ending of the 2019/20 75% Business Rates Retention pilots.

[4] DEFRA's RDEL ex budget in 2020-21 increases due to the domestic replacement of Common Agricultural Policy spending.

[5] Block grant adjustments have been agreed with the Scottish Government for tax and welfare devolution and with the Welsh Government for tax devolution as part of this respective fiscal framework.

[6] This includes the 5% needs-based Barnett formula uplift.

[7] This includes the 2.5% VAT abatement.

[8] Departmental budgets in 2020-21 include amounts carried forward from 2019-20 through Budget Exchange, which will be voted at Main Estimates. These increases will be offset at Supplementary Estimates in future years so are excluded from spending totals.

[9] The OBR's forecast of underspends in Resource DEL budgets.

## The Spending Envelope and Comprehensive Spending Review 2020

**1.51** The Budget marks the start of an ambitious programme of investment in communities across the country, many of whom feel left behind. The Budget launches the CSR, which will conclude in July.[21]

### Path of Public Spending

#### The Comprehensive Spending Review envelope

**1.52** The CSR will set Resource DEL budgets for three years to 2023-24 inclusive and Capital DEL funding for departments to 2024-25. The CSR will be delivered within the fiscal rules set out in paragraph 1.34. The Budget sets the overall spending envelope for resource and capital spending within which the CSR will be delivered. Total departmental spending is set to grow twice as fast as the economy over the CSR period. Day-to-day departmental spending is set to grow at the fastest rate over a spending review period since Spending Review 2004.

**1.53** Having left the EU, from 2021 the UK will no longer contribute to the EU budget as a Member State, leaving only payments due as part of Financial Settlement obligations. The government has accounted for this when setting its spending plans, allowing it to determine how an additional £14.6 billion[22] of spending by 2024-25 can be allocated to its domestic priorities, rather than be sent in contributions to the EU. The implementation period (IP) will end on 31 December 2020. The baseline scenario is that the UK will exit the IP at this time without a future relationship being agreed with the EU. HM Treasury will ensure that all necessary funding is made available to prepare for this outcome at the end of 2020.

**Table 1.10: Total departmental budgets (Total DEL); Resource DEL excluding depreciation and Capital DEL from 2019-20 to 2024-25[1,2,3] (£ billion, unless otherwise stated)**

| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 | AARG 2019-20 to 2024-25[4,5,6] |
|---|---|---|---|---|---|---|---|
| **Total Resource DEL excluding depreciation** | **330.4** | **360.6** | **384.6** | **400.7** | **417.6** | **435.5** | **3.3%** |
| OBR allowance for shortfall | -0.5 | -3.2 | -3.9 | -4.1 | -4.3 | -4.4 | |
| **OBR resource DEL excluding depreciation forecast** | 329.9 | 357.3 | 380.8 | 396.6 | 413.3 | 431.1 | |
| **Total Capital DEL** | **71.1** | **88.5** | **101.7** | **107.5** | **109.1** | **112.8** | **6.9%** |
| OBR allowance for shortfall | 0.0 | -3.9 | -7.3 | -7.8 | -8.0 | -8.1 | |
| **OBR capital DEL forecast** | **71.2** | **84.6** | **94.3** | **99.6** | **101.1** | **104.7** | |
| ***Total departmental spending (Total DEL)*** | **401.5** | **449.0** | **486.3** | **508.1** | **526.8** | **548.3** | **4.0%** |

[1] Budgeting totals are shown including the Office for Budget Responsibility (OBR) forecast Allowance for Shortfall.

[2] Resource DEL excluding ring-fenced depreciation is the Treasury's primary control within resource budgets and is the basis on which departmental Spending Review settlements are agreed. The OBR publishes Public Sector Current Expenditure (PSCE) in DEL and AME. A reconciliation is published by the OBR.

[3] Capital DEL is the Treasury's primary control within capital budgets and is the basis on which departmental Spending Review settlements are agreed. The OBR publishes Public Sector Gross Investment (PSGI) in DEL and AME. A reconciliation is published by the OBR.

[4] DEL in 2019-20 and 2020-21 is reduced by Business Rates Retention pilots that switched spending into AME. To ensure consistency, growth rates for Resource DEL and Capital DEL have been adjusted to reverse this DEL-AME switch.

[5] Resource DEL from 2020-21 onwards is increased by the devolution of areas of welfare spending to the Scottish Government which has caused a decrease in the Block Grant Adjustment and subsequent increase in Resource DEL. To ensure consistency, growth rates for Resource DEL and Capital DEL have been adjusted to reverse this switch.

[6] Capital DEL from 2020-21 onwards includes a provision for the impact of the IFRS16 reclassification of leases on departmental capital budgets. To ensure consistency, growth rates have been adjusted to reverse this provision.

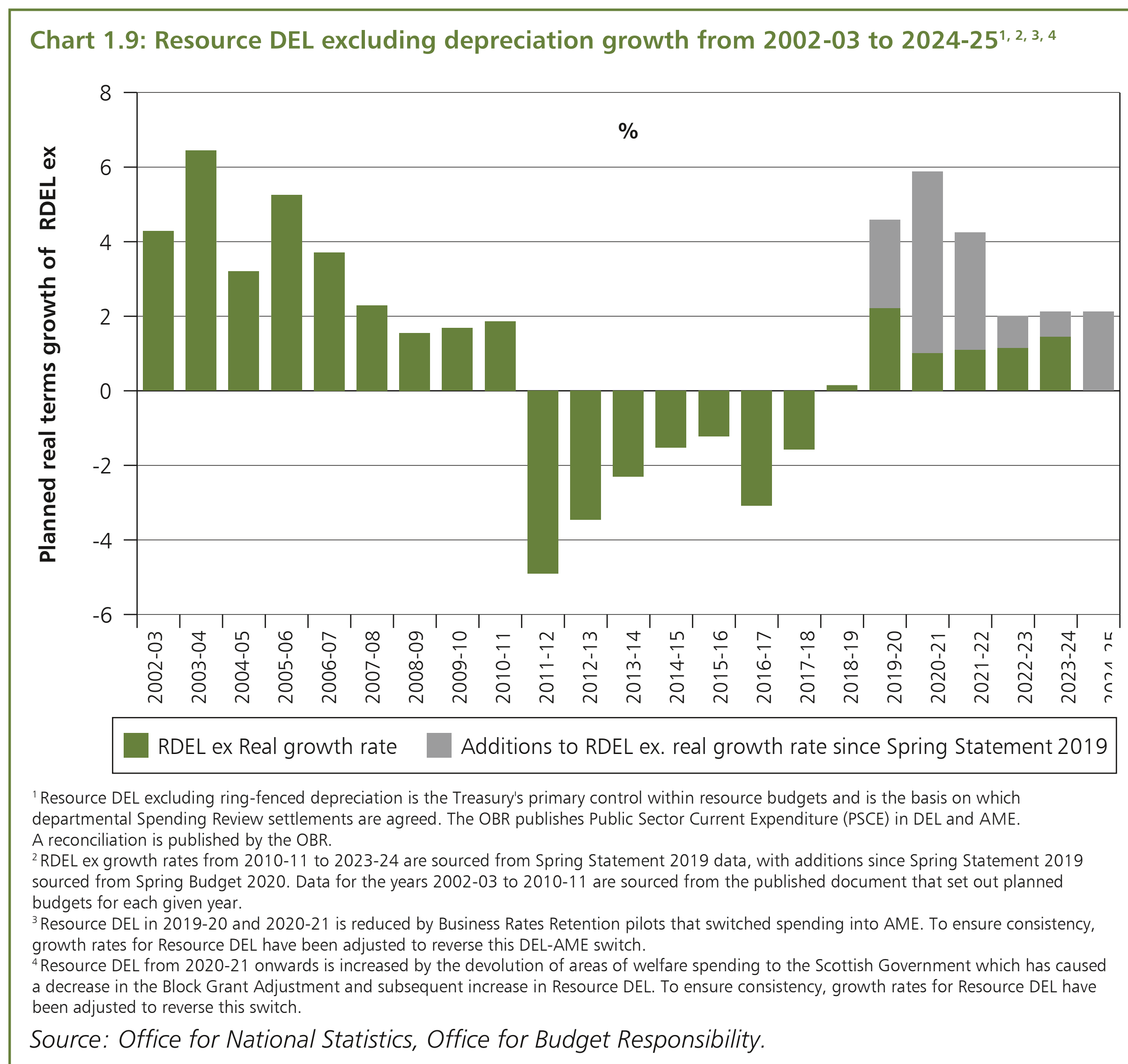
[21] The government will keep the timing of the CSR under review in the coming weeks, given the inherent uncertainty over the operational impact of COVID-19.

[22] The OBR have removed the assumed spending in lieu of EU transfers from the forecast. This is a difference of £4.3 billion, increasing to £14.6 billion by the end of the forecast period.

### Resource

**1.54** The CSR will see an increase in day-to-day spending from £360.6 billion in 2020-21 to £417.6 billion by 2023-24. Overall Resource DEL spending will increase by 2.8% per year on average in real terms over the CSR period. Over the Parliament, it will grow by 3.3% on average in real terms. Chart 1.9 shows the real terms growth in day-to-day departmental spending over the forecast period.

**Chart 1.9: Resource DEL excluding depreciation growth from 2002-03 to 2024-25**[1, 2, 3, 4]




[1] Resource DEL excluding ring-fenced depreciation is the Treasury's primary control within resource budgets and is the basis on which departmental Spending Review settlements are agreed. The OBR publishes Public Sector Current Expenditure (PSCE) in DEL and AME. A reconciliation is published by the OBR.
[2] RDEL ex growth rates from 2010-11 to 2023-24 are sourced from Spring Statement 2019 data, with additions since Spring Statement 2019 sourced from Spring Budget 2020. Data for the years 2002-03 to 2010-11 are sourced from the published document that set out planned budgets for each given year.
[3] Resource DEL in 2019-20 and 2020-21 is reduced by Business Rates Retention pilots that switched spending into AME. To ensure consistency, growth rates for Resource DEL have been adjusted to reverse this DEL-AME switch.
[4] Resource DEL from 2020-21 onwards is increased by the devolution of areas of welfare spending to the Scottish Government which has caused a decrease in the Block Grant Adjustment and subsequent increase in Resource DEL. To ensure consistency, growth rates for Resource DEL have been adjusted to reverse this switch.

*Source: Office for National Statistics, Office for Budget Responsibility.*

### Capital

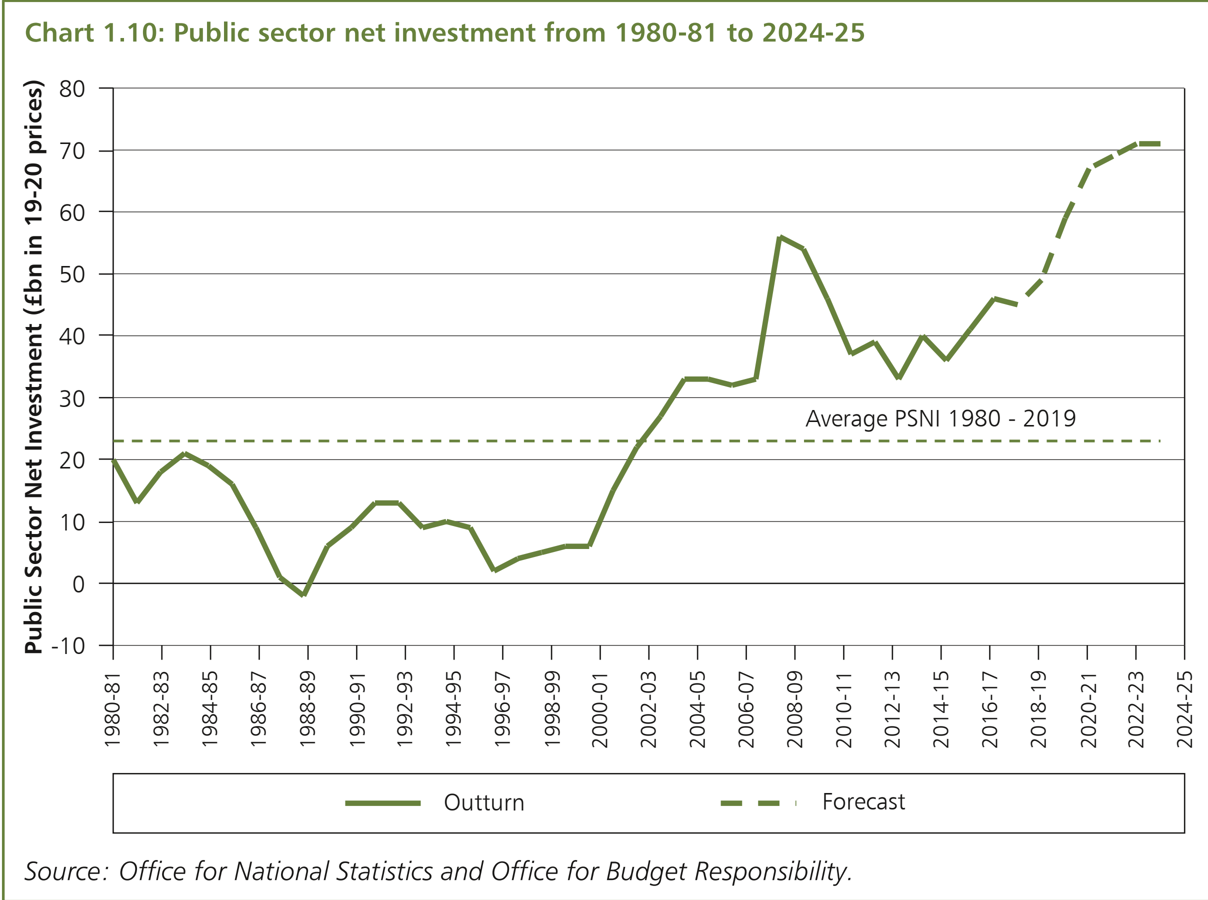
**1.55** Over the next five years the public sector will invest £640 billion, as set out in Table 1.11. This significant increase in spending means that by 2024-25, public sector net investment will be triple the average investment over the last 40 years in real terms, as shown in Chart 1.9.

**1.56** This spending will provide world-class infrastructure and public services, delivering value for money and focussing on efficient delivery. The CSR will allocate capital funding for projects across the UK to drive growth, level up economic opportunity, decarbonise the economy, and maintain and build high quality public infrastructure, including schools and hospitals. The Budget sets out plans to increase public R&D investment to £22 billion per year by 2024-25, taking public spending on R&D to 0.8% of GDP.

**1.57** These allocations will be informed by early findings from the review of HM Treasury's Green Book, which will consider how the design and use of project appraisal affects the ability of all areas to achieve their economic potential. The review will enhance the strategic

development and assessment of projects, consider how to assess and present local impacts and look to develop new analytical methods for transformative or place-based interventions. It will also consider how project approval decisions are being made and provide clearer guidance and support to practitioners. The government will work with users, academics and others, and a revised Green Book will be published alongside the CSR.

**Chart 1.10: Public sector net investment from 1980-81 to 2024-25**




*Source: Office for National Statistics and Office for Budget Responsibility.*

## Total managed expenditure

**1.58** These firm decisions on the Departmental Expenditure Limits (DEL) envelope for the CSR mean that the average annual real growth of Total Managed Expenditure (TME), the total amount of money that the government spends through departments, local authorities, other public bodies and social security, will be 1.9% between 2019-20 and 2024-25. Table 1.11 sets out planned TME, public sector current expenditure (PSCE) and public sector gross investment (PSGI) up to 2024-25. Chart 1.11 which shows the change in government spending as a share of GDP over time, shows that tough decisions made in the aftermath of the financial crisis have restored the public finances to health and the government can now afford to invest more in public services and growing the economy.

**1.59** Government spending is now set to be 40.7% of GDP in 2024-25. TME as a percentage of GDP has also increased because of classification and methodology changes that have impacted underlying spending, in particular those relating to student loans, public sector pensions and depreciation.[23] These are technical revisions that have been applied to the entire time series of data to ensure comparison to other years can be done on an equal basis.

[23] Public Sector Finances, UK: August 2019; Office for National Statistics; September 2019

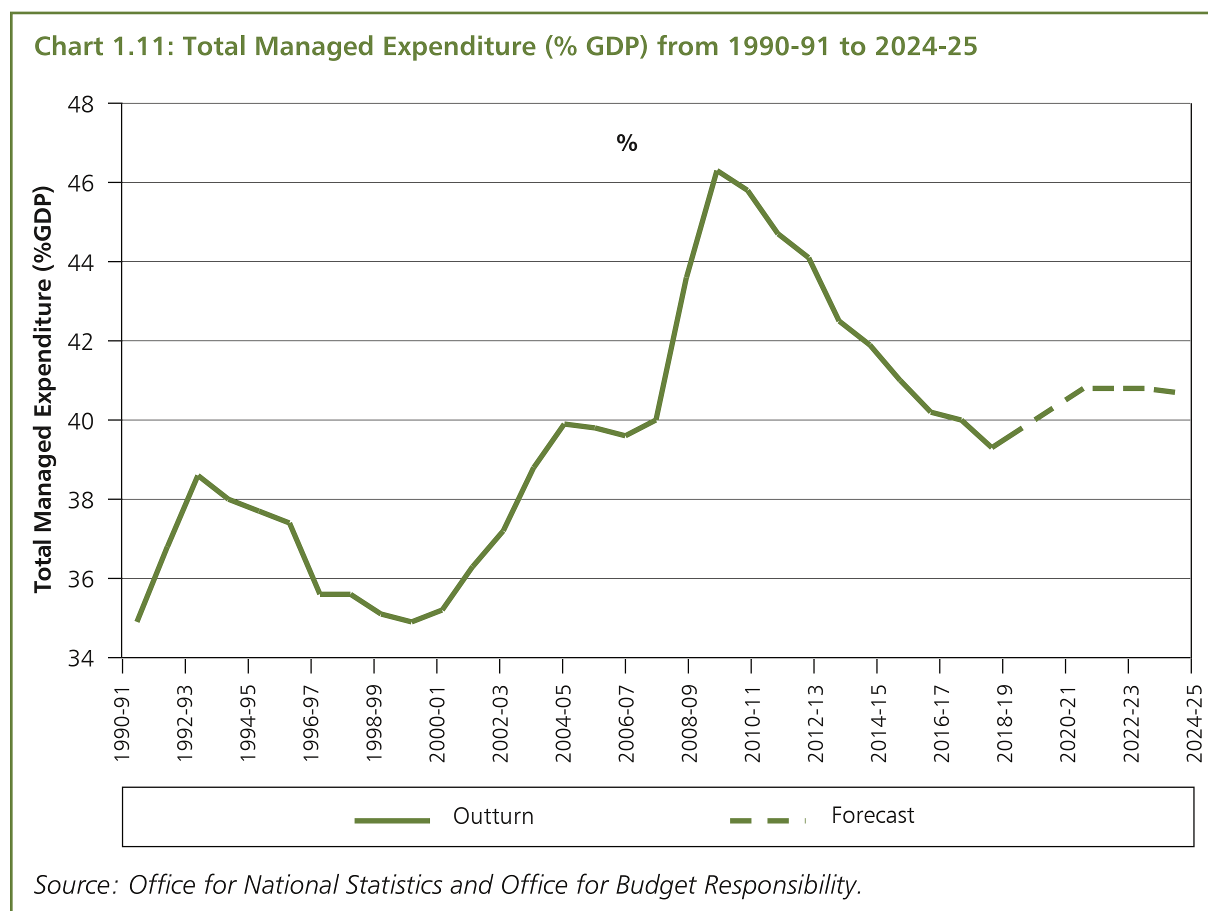
**Table 1.11: Total Managed Expenditure[1] from 2019-20 to 2024-25 (in £ billion, unless otherwise stated)**

| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| **Current expenditure** | | | | | | |
| Resource AME | 426.5 | 421.6 | 433.5 | 443.4 | 453.2 | 464.7 |
| Resource DEL excluding depreciation | 330.4 | 360.6 | 384.6 | 400.7 | 417.6 | 435.5 |
| Ring-fenced depreciation | 30.8 | 33.6 | 35.9 | 37.4 | 39.0 | 40.6 |
| **Total public sector current expenditure** | **787.7** | **815.8** | **854.1** | **881.5** | **909.9** | **940.8** |
| **Capital expenditure** | | | | | | |
| Capital AME | 33.6 | 30.4 | 26.6 | 26.9 | 28.5 | 29.2 |
| Capital DEL excluding financial transactions | 65.5 | 81.6 | 96.7 | 102.3 | 106.5 | 110.2 |
| **Total public sector gross investment** | **99.1** | **111.9** | **123.3** | **129.2** | **135.0** | **139.4** |
| **Total managed expenditure** | **886.8** | **927.7** | **977.4** | **1010.7** | **1044.9** | **1080.2** |
| *Total managed expenditure % of GDP* | *39.8%* | *40.3%* | *40.8%* | *40.8%* | *40.8%* | *40.7%* |

[1] Budgeting totals are shown including the Office for Budget Responsibility (OBR) forecast Allowance for Shortfall. Resource DEL excluding ring-fenced depreciation is HM Treasury's primary control within resource budgets and is the basis on which departmental Spending Review settlements are agreed. The OBR publishes Public Sector Current Expenditure (PSCE) in DEL and AME, and PSGI in DEL and AME. A reconciliation is published by the OBR.

*Source: Office for Budget Responsibility and HM Treasury calculations.*

**Chart 1.11: Total Managed Expenditure (% GDP) from 1990-91 to 2024-25**




*Source: Office for National Statistics and Office for Budget Responsibility.*

## Allocations for the Comprehensive Spending Review

**1.60** Chapter 2 of this document sets out further detail on the allocations made at the Budget. The overall allocations of total resource and capital funding over the CSR period will be determined at the CSR in July.

**1.61** The CSR will prioritise:

- levelling up economic opportunity across all nations and regions of the country by investing in infrastructure, innovation and people, to drive productivity and spread opportunity
- improving outcomes in public services, including supporting the NHS and taking steps to cut crime and ensure every young person receives a superb education
- strengthening the UK's place in the world
- reducing carbon emissions and improving the natural environment

**1.62** All new spending will be accompanied by a rigorous new focus on outcomes. To support this the government is conducting an exercise across departments to identify savings and projects that do not provide value for money or support these priorities. The government will redirect this spending through the CSR to help achieve its priorities. The CSR will also set out plans to improve the use of data, science and technology across the public sector, and to ensure all programmes are supported by robust implementation and evaluation plans.

**1.63** In conducting the CSR, the government will also build on the lessons of previous spending reviews and ensure that policy issues are considered across departmental boundaries to maximise the effectiveness and value for money of government spending. The Budget announces the first allocation from the Shared Outcomes Fund to pilot improved approaches to supporting adults with complex needs. This fund was established at Spending Round 2019 to pilot new programmes to build an evidence base and test new ways of working collaboratively across the public sector. Further details on this bid can be found in Chapter 2.

**1.64** The CSR will be informed by the Integrated Security, Defence, Development and Diplomacy Review (Integrated Review). The government intends to publish the main conclusions of the Integrated Review alongside the CSR.

**1.65** At the CSR the government will set out funding to meet commitments to replace the Common Agricultural Policy and EU structural funds. The government may also choose to participate in certain EU programmes, where it is in UK interests and the contributions are fair and appropriate.

## Improving public services

### Priority outcomes and evaluation

**1.66** The government's spending plans provide for significant real increases in spending on public services. It is crucial that increased government funding leads to real-world improvements that make a difference to people's lives. At the CSR, the government will establish a new approach to link departments' spending proposals to the outcomes they intend to achieve as part of a new Public Value Framework (PVF).[24]

**1.67** The government is developing the medium- to long-term priority outcomes that it is seeking to deliver for priorities such as levelling up, as well as the metrics that will be used to measure and improve performance against these outcomes. Assessment of spending's impact on these priority outcomes will be central to making spending decisions at the CSR. These priority outcomes and metrics will be published as part of the CSR and will include cross-cutting outcomes in areas where closer working between departments could help achieve better results.

[24] 'Public Value Framework and supplementary guidance'; HM Treasury; March 2019

**1.68** In order to ensure government programmes deliver for the public, it is crucial that spending decisions are based on robust evidence and evaluation of their impact. At the CSR, the government will assess the state of evaluation across all departmental spending programmes and require every department to produce plans to improve evaluation of its work. This will lead to more evidence-based allocation of public funding and better outcomes in the long term.

**1.69** These reforms will ensure that spending decisions are based on the delivery of outcomes and will put the UK at the forefront of international approaches to driving public value. This will help the government provide world-class public services and the best value for taxpayers' money.

### Public representations

**1.70** Throughout the CSR the government will engage with all regions and nations of the UK to ensure that its policies level up and spread opportunity. The government has started this engagement at Budget by launching a process for individuals and organisations to submit written CSR representations to HM Treasury.

### Financial transactions

**1.71** Some policy measures do not directly affect PSNB in the same way as conventional spending or taxation. These include financial transactions, which predominantly affect the central government net cash requirement (CGNCR) and public sector net debt (PSND). Table 1.12 shows the effect of the financial transactions announced since Budget 2018 on CGNCR. Details on the policy decisions made at the Budget can be found in Chapter 2.

**Table 1.12: Financial transactions from 2019-20 to 2024-25 (£ million)[1,2]**

| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| Ending student loan sales programme | -2,125 | -1,860 | -1,740 | -1,420 | 1,985 | 1,985 |
| UKAR pension scheme | 0 | 0 | 0 | 0 | 240 | -35 |
| VAT: cash flow impact of postponed accounting | 0 | -3,555 | -180 | 910 | 295 | -35 |
| Freezing the maximum tuition fee cap: 2020-21 | 0 | 140 | 280 | 295 | 315 | 325 |
| Entitlement to part-time maintenance loans | 90 | 220 | 350 | 445 | 505 | 555 |
| Nurse maintenance grants: student finance implication | 0 | -15 | -65 | -125 | -175 | -190 |
| Removing student finance residence requirement for domestic abuse victims | 0 | neg | -5 | -5 | -5 | -5 |
| Increase to UK Export Finance Direct Lending Facility | 0 | -250 | -445 | -685 | -435 | -180 |
| Help to Buy: policy definition | 0 | -65 | 570 | 650 | 0 | 0 |
| Universal Credit: extending advances repayment period and reducing maximum debt deductions | 0 | 0 | -15 | -165 | -100 | -85 |
| British Business Bank: Start Up Loans | 0 | 0 | -115 | 25 | 25 | 20 |
| British Business Bank: Life Sciences Investment Programme | 0 | -10 | -30 | -35 | -30 | -15 |
| British Business Bank: growth capital for innovative business | 0 | -55 | -95 | -70 | -50 | -15 |
| National Security Strategic Investment Fund | 0 | -50 | 0 | 0 | 0 | 0 |
| Heat Networks Investment Project | 0 | 0 | -70 | 0 | 0 | 0 |
| Nature for Climate Fund | 0 | -10 | 0 | 0 | 0 | 0 |
| **Total policy decisions** | **-2,035** | **-5,510** | **-1,560** | **-180** | **2,570** | **2,325** |

Note: This table details new financial transactions scored at this Budget

[1] Costings reflect the Office for Budget Responsibility's latest economic and fiscal determinants, and are presented on a UK basis.

[2] Negative numbers in the table represent a cost to the Exchequer.

## Devolved administrations

**1.72** The application of the Barnett formula to spending decisions taken by the UK government at the Budget will provide each of the devolved administrations with additional funding to be allocated according to its own priorities. To reflect the additional powers devolved to the Scottish and Welsh Governments their block grants will be adjusted as set out in their respective fiscal frameworks. This includes a substantial increase in the Scottish Government's block grant to reflect the additional welfare responsibilities being devolved from April 2020. The Scottish and Welsh Governments have already set provisional budgets for 2020-2021 using block grant adjustments based on previous OBR forecasts. They have been given the choice of taking on the updated block grant adjustments following the UK Budget or waiting for the outturn reconciliation processes that will take place after the end of 2020-2021.

**1.73** While all block grant funding remains in DEL, the Scottish Government now has such substantial self-funding powers (from taxation, borrowing and reserves) that its spending is recorded in Annually Managed Expenditure (AME).

## Welfare cap

**1.74** The welfare cap was introduced in 2014 to limit the amount spent on certain social security benefits and tax credits. It improves Parliamentary accountability for welfare spending and supports the government's aim of ensuring the welfare system is sustainable.

**1.75** The cap was last reset at Autumn Budget 2017, following the OBR's judgement that the government had successfully met the terms of the welfare cap set at Autumn Statement 2016. The cap applies to spending within its scope in 2022-23, with a 3% margin of flexibility to manage unavoidable fluctuations in spending.

**1.76** In accordance with the Charter for Budget Responsibility, as is mandated for the first fiscal event of the Parliament, the OBR has formally assessed spending against the welfare cap in its 'Economic and fiscal outlook'. Total relevant spending is forecast to be within the welfare cap and margin, and so the fiscal rule is judged to have been met with £3.4 billion of headroom.

**1.77** The government is now required to reset the welfare cap for the new Parliament. The cap will be based on the OBR's Budget forecast of the benefits and tax credits in scope, as set out in Annex B, and will apply to spending in 2024-25. In the interim years, progress towards the cap will be managed internally, based on monitoring by HM Treasury and the Department for Work and Pensions (DWP) of the OBR's welfare spending forecasts. As before, there will be a margin rising to 3% above the forecast to manage unavoidable fluctuations in spending. The cap will be breached if spending exceeds the cap plus the margin at the point of assessment. Performance against the cap will be formally assessed by the OBR at the first fiscal event of the next Parliament. This will avoid the government having to make short-term responses to changes in the welfare forecast, while ensuring welfare spending remains sustainable in the medium term.

**Table 1.13: New welfare cap (in £ billion, unless otherwise stated)**

| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| Cap | - | - | - | - | - | 137.2 |
| Interim pathway | 119.3 | 125.7 | 127.5 | 130.5 | 133.8 | - |
| Margin (%) | 0.5 | 1.0 | 1.5 | 2.0 | 2.5 | 3.0 |
| Cap, pathway and margin | 119.9 | 127.0 | 129.5 | 133.1 | 137.1 | 141.3 |

*Source: HM Treasury.*

## Debt and reserves management

**1.78** The government's financing plans for 2020-21 are summarised in Annex A. They are set out in full in the 'Debt management report 2020-21', published alongside the Budget.

## Supporting those affected by COVID-19

**1.79** Since emerging in China in December 2019, COVID-19 has spread widely, with a significant number of cases reported worldwide, including an increasing number in the UK.

**1.80** The impact of the outbreak of COVID-19 on the UK economy is highly uncertain, and while the effect could prove significant, it is expected to be temporary.

**1.81** As an open economy, the UK will be affected because of the wider impacts the outbreak is having on the global economy. In a domestic outbreak, there could also be direct economic impacts in the UK driven by health-related factors, including how many people are infected and the persistence of any outbreak. Disruption could include temporary absences from work and interruptions to global supply chains, both of which would constrain the UK's productive capacity for a temporary period. In addition, the economy could be affected by demand-side impacts through a reduction in consumer spending, and lower business investment and exports. The government's Action Plan on Coronavirus sets out the potential scale of these effects in the event of a severe outbreak.

**1.82** The government recognises that people will be concerned about the impact COVID-19 could have on their lives, and some businesses will be concerned about reduced demand, potential disruptions to supply chains and export markets, and to their workforce during this temporary period. Therefore, the Budget announces a three-point plan to provide support for:

- public services
- individuals
- businesses

**1.83** The plan includes a range of timely, targeted and temporary measures to deliver support when and where it is needed, at a total cost of £12 billion. The wider Budget policy decisions set out in Table 2.1 represent £18 billion of additional government spending, which will provide support to the economy. Together, the government is taking £30 billion of policy action in 2020-21, equivalent to approximately 1.3% of GDP.

**1.84** In addition to the measures set out here, the government will continue to monitor the situation and stands ready to provide further support, should it be needed. Support will be available for as long as it is needed, based on the latest scientific evidence. HM Treasury will continue to work closely with the Bank of England to coordinate the response of the UK authorities to ensure it is as effective as possible.

**1.85** The government is working closely with the devolved administrations on this issue and it stands ready to provide further support. Where measures do not apply UK-wide, the devolved administrations will receive a share of any additional funding for support in devolved areas through the Barnett Formula. As set out in the Statement of Funding Policy the devolved administrations can also access the Reserve where they are unable to manage any disproportionate costs from their own resources.

**1.86** The government welcomes the statement by UK Finance on behalf of the sector which announced that banks, building societies and credit card providers are ready and able to offer support to consumers, including offering or increasing an overdraft or allowing repayment relief for loan or mortgage repayments. Banks and other providers of SME finance will also provide support for businesses that are facing cash flow disruption and stand ready to help when needed.

**1.87** Tackling COVID-19 is a global challenge. To complement its domestic response, the UK is leading the way to ensure a swift and effective global response, including by working closely with all our international partners and supporting the most vulnerable countries to deal with the impacts of the virus, including cooperating closely with counterparts in the G7 and G20.

**1.88** The Chancellor will continue to co-operate closely with his counterparts in the G7 and G20. G20 Finance Ministers last week committed to monitoring the evolution of COVID-19 including its impact on markets and economic conditions, and highlighted their readiness to take further actions to aid in the response to the virus, support the economy and maintain the resilience of the financial system.

## Support for public services

**1.89** Public safety is the government's top priority in its response to COVID-19. The government will ensure that public services receive the funding they need to respond to the outbreak as the situation develops. This includes continuing to ensure our health services have the resources they need to respond.

**1.90 COVID-19 response fund** – HM Treasury is creating an emergency response fund, set aside to ensure the National Health Service (NHS) and other public services have the resources they need to tackle the impacts of COVID-19. Initially set at £5 billion, it will fund pressures in the NHS, support local authorities to manage pressures on social care and support vulnerable people, and help deal with pressures on other public services. The size of the fund will be reviewed as the situation develops, to ensure all necessary resources are made available.

**1.91 Funding for research and development** – The government is providing the National Institute for Health Research with £30 million of new funding to enable further rapid research into the disease. Research is essential in order to understand COVID-19, and it will inform how the NHS frontline service approach tackling the virus. The funding could also allow rapid screening of potential therapeutics and support clinical trials to inform treatment and improve patient outcomes.

**1.92 Funding for diagnostic testing** – The government will increase the capacity and capability of diagnostic testing and surveillance facilitated by Public Health England to support the NHS, by providing an additional £10 million of new funding to DHSC.

## Support for individuals

**1.93** The Budget announces measures to support people who are unable to work because of COVID-19.

**1.94 Eligibility for Statutory Sick Pay (SSP)** – The Prime Minister has already announced that the forthcoming COVID-19 Bill will temporarily allow SSP to be paid from the first day of sickness absence, rather than the fourth day, for people who have COVID-19 or have to self-isolate, in accordance with government guidelines. The Budget sets out a further package to widen the scope of SSP and make it more accessible. The government will temporarily extend SSP to cover:

- individuals who are unable to work because they have been advised to self-isolate
- people caring for those within the same household who display COVID-19 symptoms and have been told to self-isolate

**1.95 Medical Evidence for SSP** – The government has already issued guidance to employers, advising them to use their discretion not to require a GP fit note for COVID-19 related absences. This Budget announces that the government and the NHS will bring forward a temporary

alternative to the fit note in the coming weeks which can be used for the duration of the COVID-19 outbreak. This system will enable people who are advised to self-isolate to obtain a notification via NHS111 which they can use as evidence for absence from work, where necessary. This notification would meet employers' need for evidence, whilst taking pressure away from General Practices.

**1.96 Support for those ineligible for SSP** – The government recognises that self-employed people and employees below the Lower Earnings Limit are not entitled to SSP. The best system of financial support for these people is the welfare system and, in particular, 'new style' Employment and Support Allowance and Universal Credit. The government is committed to supporting these groups, and the Budget announces further support by making it quicker and easier to receive benefits:

- 'New style' Employment and Support Allowance will be payable for people directly affected by COVID-19 or self-isolating according to government advice for from the first day of sickness, rather than the eighth day
- people will be able to claim Universal Credit and access advance payments where they are directly affected by COVID-19 (or self-isolating), without the current requirement to attend a jobcentre
- for the duration of the outbreak, the requirements of the minimum income floor in Universal Credit will be temporarily relaxed for those directly affected by COVID-19 or self-isolating according to government advice for duration of the outbreak, ensuring self-employed claimants will be compensated for losses in income

**1.97 Hardship Fund** – The government will provide Local Authorities in England with £500 million of new grant funding to support economically vulnerable people and households in their local area. The government expects most of this funding to be used to provide more council tax relief, either through existing Local Council Tax Support schemes, or through complementary reliefs.

## Support for businesses

**1.98** Some businesses may experience increased costs or disruptions to their cash flow as a result of COVID-19. The Budget announces a set of measures to provide support to businesses during this temporary period by either reducing their costs or bridging cashflow problems arising from the outbreak, and to protect people's jobs.

**1.99 Statutory Sick Pay** – The government will support small and medium-sized businesses and employers to cope with the extra costs of paying COVID-19 related SSP by refunding eligible SSP costs. The eligibility criteria for the scheme are as follows:

- this refund will be limited to two weeks per employee
- employers with fewer than 250 employees will be eligible. The size of an employer will be determined by the number of people they employed as of 28 February 2020
- employers will be able to reclaim expenditure for any employee who has claimed SSP (according to the new eligibility criteria) as a result of COVID-19
- employers should maintain records of staff absences, but should not require employees to provide a GP fit note
- the eligible period for the scheme will commence from the day on which the regulations extending SSP to self-isolators come into force

- while existing systems are not designed to facilitate such employer refunds for SSP, the government will work with employers over the coming months to set up a repayment mechanism for employers as soon as possible

**1.100 Business Rates Reliefs** – The government has already announced the Business Rates retail discount will be increased to 50% in 2020-21. To support small businesses affected by COVID-19 the government is increasing it further to 100% for 2020-21. The relief will also be expanded to the leisure and hospitality sectors. These temporary measures, taken together with existing Small Business Rates Relief, mean that around 900,000 properties, or 45% of all properties in England, will receive 100% business rates relief in 2020-21. The government has also already announced the introduction of a £1,000 Business Rates discount for pubs with a rateable value below £100,000 in England for one year from 1 April 2020. To support pubs in response to COVID-19 the discount will be increased to £5,000. Local authorities will be fully compensated for these Business Rates measures.

**1.101 Small business grant funding** – The government recognises that many small businesses pay little or no business rates because of Small Business Rate Relief (SBRR). To support those businesses, the government will provide £2.2 billion of funding for Local authorities in England. This will provide £3,000 to around 700,000 business currently eligible for SBRR or Rural Rate Relief, to help meet their ongoing business costs. For a property with a rateable value of £12,000, this is one quarter of their rateable value, or comparable to 3 months of rent. Most properties that are eligible for SBRR will have a lower rateable value, and so this will represent an even greater proportion of their annual rent.

**1.102 Time to Pay** – The government will ensure that businesses and self-employed individuals in financial distress and with outstanding tax liabilities receive support with their tax affairs. Her Majesty's Revenue and Customs (HMRC) has set up a dedicated COVID-19 helpline to help those in need, and they may be able to agree a bespoke Time to Pay arrangement. Time to Pay was successfully used in response to flooding and the financial crisis, giving businesses a time-limited deferral period on HMRC liabilities owed and a pre-agreed time period to pay these back. These tailored arrangements will give a business the time it needs to pay HMRC to support their recovery while operating through any temporary financial challenges that occur. To ensure ongoing support, HMRC have made a further 2,000 experienced call handlers available to support firms when needed. HMRC will also waive late payment penalties and interest where a business experiences administrative difficulties contacting HMRC or paying taxes due to COVID-19.

**1.103 Coronavirus Business Interruption Loan Scheme** – The government will launch a new, temporary Coronavirus Business Interruption Loan Scheme, delivered by the British Business Bank, to support businesses to access bank lending and overdrafts. The government will provide lenders with a guarantee of 80% on each loan (subject to a per lender cap on claims) to give lenders further confidence in continuing to provide finance to SMEs. The government will not charge businesses or banks for this guarantee, and the Scheme will support loans of up to £1.2 million in value. This new guarantee will initially support up to £1 billion of lending on top of current support offered through the British Business Bank.

## International response

**1.104** The government has already committed £91 million to the international response. The Budget makes available £150 million from the UK's ODA budget to the International Monetary Fund's Catastrophe Containment and Relief Trust (CCRT), of which £75 million, with an immediate commitment of £75 million. This demonstrates that the UK can use its ODA budget to directly support our national interest. The government stands ready to provide further support as the situation develops, playing our full part in a well-coordinated global response.

**1.105** Alongside the Budget, the government has published information about the support available to individuals and businesses whose finances are affected by COVID-19. This information, which will be regularly updated as the situation develops, can be found at: https://www.gov.uk/government/publications/support-for-those-affected-by-covid-19.

# Investing in excellent public services

**1.106** The government is delivering world-class public services for hard-working people across the UK. The Budget builds on the significant investment in public services made at Spending Round 2019, with action to make the UK a safer, healthier place to live.

## Investing in the NHS

**1.107** The NHS is the government's number one spending priority. The NHS settlement, confirmed in January 2019, provided the largest cash increase in public services since the Second World War – an additional £34 billion per year by 2023-24.[25] Spending Round 2019 confirmed the government's commitment to the NHS, with £139 billion for health budgets in 2020-21.[26] The Budget provides over £6 billion of further funding to strengthen the NHS in England and pay for vital services that will improve people's health, reaffirming the government's commitment to health and social care.

**1.108** The government will invest to increase staffing, making sure that the NHS has the people it needs. This will include **a significant funding package to improve the recruitment, training and retention of nurses** in England, ensuring there are 50,000 more in the NHS; and for the recruitment, training and retention of up to 6,000 more GPs and 6,000 more primary care professionals in England, such as physiotherapists and pharmacists. This will **create 50 million more GP surgery appointments a year**. The government will also **change pensions tax rules to ensure that NHS staff across the UK, including senior doctors, whose income is less than £200,000 can work additional hours for the NHS without their annual allowance being reduced**. (7)

**1.109** The government will invest in our hospitals, including **over £100 million in 2020-21 to make progress on 40 new hospital projects**, as part of a long-term programme of investment in health infrastructure to ensure the NHS has world-class facilities for patients.[27] This will be accompanied by an increase in DHSC's capital budget of £683 million in the 2020-21 financial year to **protect the level of NHS operational capital investment**. This will allow Trusts to continue to invest in important capital projects such as estate refurbishments and building maintenance. (5)

**1.110** To ensure that new arrivals to the UK contribute to the funding of the NHS, the Immigration Health Surcharge will be increased to £624. The government will also introduce a new discounted rate of £470 for children in recognition of the increased financial impact on family groups. (6)

**1.111** The government is committed to long-term reform of adult social care and the Secretary of State for Health and Social Care has written to parliamentarians to begin building cross-party consensus on reform. Ahead of those discussions, **the government will invest £1 billion of additional funding for social care next year, as announced at Spending Round 2019**. The Budget confirms that this additional funding will continue for every year of the current Parliament to continue to stabilise the system.

[25] 5 year NHS funding plan, Department of Health and Social Care, Her Majesty's Treasury, June 2018
[26] Spending Round 2019, Her Majesty's Treasury, September 2019
[27] Health Infrastructure Plan, Department of Health and Social Care, September 2019

## Supporting schools and young people

**1.112** At Spending Round 2019, the government committed to a £7.1 billion cash increase in funding for schools in England by 2022-23, compared to 2019-20 budgets. This funding settlement included an increase to minimum per-pupil funding levels, a commitment now enshrined in law.[28] The minimum per pupil amount will increase to £3,750 for primary schools and £5,000 for secondary schools in 2020-21, with the primary schools minimum then rising to £4,000 in 2021-22.[29] The settlement also provides for £780 million extra in 2020-21 to support children and young people with special educational needs, to ensure all can reach their potential.

**1.113** On average, schools will see an increase of over 4% in funding per pupil compared to 2019-20 budgets.[30] The three-year settlement will also allow the government to raise starting salaries for teachers to £30,000 by September 2022.

**1.114** This funding settlement reflects the government's commitment to high quality education for all school children. The Budget sets out new steps the government is taking to support children to have the opportunity of an active and enriching school experience.

**1.115** To ensure that children get an active start in life, the government will bring forward an updated School Sport and Activity Action Plan following the Comprehensive Spending Review. Ahead of that, the Budget provides **£29 million a year by 2023-24 to support primary school PE teaching and help schools make best use of their sports facilities**. The funding will support high quality teacher training and professional development for PE, informed by best practice PE teaching.

**1.116** The government also believes in the benefits of participating in the arts and the essential role it plays in all children's education. The Budget provides **£90 million a year to introduce an Arts Premium from September 2021**, averaging out as an extra £25,000 a year per secondary school for three years.[31] The funding will help schools to provide high quality arts programmes and extracurricular activities for pupils, including those delivered in partnership with arts organisations, as well as supporting teachers to deliver engaging and creative lessons in the arts.

## Ensuring people's safety and security

**1.117** Protecting people and keeping them safe from crime and other threats is a principal responsibility of any government. The government announced an extra £750 million of funding at the 2019 Spending Round to begin the recruitment of 20,000 additional police officers, with the first 6,000 officers to be recruited by March 2021. The Budget makes further important investments in the police, security services and justice system.

**1.118** In addition, the Budget will include £114 million in 2020-21 for counter-terrorism, to maintain capability and officer numbers in the face of a changing terrorist threat. This includes an extra £83 million for counter-terrorism policing, in addition to the government's police recruitment commitment, and £31 million for the UK Intelligence Community. The government will also provide an additional **£67 million for the UK Intelligence Community** which will enable them to develop further their world-leading technological capabilities to protect the UK's security and help keep the country safe. (9)

---

[28] Minimum funding levels for schools, Department for Education, January 2020

[29] National funding formula tables for schools and high needs: 2020 to 2021, Department for Education, October 2019

[30] ibid.

[31] Schools, pupils and their characteristics: January 2019, Department for Education, June 2019

**1.119** The government is committed to increasing support for victims of crime in their experience of the criminal justice system. The government will provide **an additional £15 million to improve our offer to victims**. This will boost the support available to victims of rape and create a new digital hub to make the criminal justice process in England and Wales easier to understand. The government will also provide an additional **£5 million to begin a trial of domestic abuse courts** in England and Wales, allowing criminal and family matters to be considered together. To protect victims of severe domestic abuse and their children and reduce the number of serial perpetrators, the government will provide **£10 million for innovative new approaches to preventing domestic abuse, working with Police and Crime Commissioners to expand projects like the "Drive" prevention programme**.

**1.120** The Budget contains an additional £5 million for the Youth Endowment Fund to support the **creation of a Centre of Excellence for Tackling Youth Violence**. This will create a single evidence hub on what works to divert young people away from criminal activity and improve the effectiveness of our wider investments in crime reduction, including the work of the Youth Endowment Fund and violence reduction units. The Budget will also provide £68.5 million to toughen community sentences, including by **increasing the number of offenders who are required to wear an electronic tag.**

**1.121** The government will also provide **£20 million for Fire and Rescue Services** to enable them to increase fire inspection and enforcement capability and to build capacity to respond to the Grenfell Tower Inquiry's findings, by investing in training, equipment and a stronger strategic centre for the fire service.

## Improving local services and infrastructure

**1.122** The government is committed to supporting the work of local authorities, in delivering high quality local services in communities across the country. The 2020-21 local government finance settlement enables a 6.3% nominal increase in councils' Core Spending Power.[32]

**1.123** Local authorities also invest billions of pounds of capital finance every year in their communities. The government supports this activity, in part, by offering low cost loans through the Public Works Loan Board (PWLB). However, in recent years a minority of councils have used this cheap finance to buy very significant amounts of commercial property for rental income, which reduces the availability of PWLB finance for core local authority activities. To address this **the government will consult on revising the terms of PWLB lending to ensure LAs continue to invest in housing, infrastructure and front-line services**. To further enable high quality investment by local authorities, the government is **cutting the interest rates for investment in social housing by 1 percentage point, and making an extra £1.15 billion of discounted loans available** for local infrastructure projects. (11)

**1.124** Further details and additional announcements relating to public services can be found in Chapter 2.

[32] Core spending power: provisional local government finance settlement 2020 to 2021, Ministry of Housing, Communities and Local Government, December 2019.

# Levelling up and getting Britain building

**1.125** The Budget sets out the next stage of the government's comprehensive plan to level up opportunity and share prosperity across the UK. The only sustainable way to drive economic growth and improve living standards in every corner of the country is to boost productivity. The government is therefore investing in people and places – by taking the first steps in its plan to level up skills across the country, ahead of setting out further details at the CSR, and by committing record levels of investment to infrastructure that will directly support productivity. These actions will boost national growth as well as addressing economic and social disparities and restoring the fabric of our towns and cities.

## Infrastructure

**1.126** Infrastructure underpins the economy: it is essential for markets to function effectively, it supports jobs, attracts investment, and it matters to families, communities, towns and cities. **Later in the spring the government will publish a landmark National Infrastructure Strategy** which will set out plans for a once in a generation transformation of the UK's economic infrastructure.

### Strategic transport projects

**1.127** The government is transforming regional connections through the largest ever investment in England's motorways and major A roads.[33] **The second Road Investment Strategy (RIS2) will spend over £27 billion between 2020 and 2025.** It will take forward schemes such as dualling the A66 Trans-Pennine and upgrading the A46 Newark bypass to address congestion, and building the Lower Thames Crossing to increase road capacity across the Thames east of London by 90%.[34] RIS2 will be delivered alongside the government's plans for decarbonising the transport sector, which are set out in the 'Growing a greener economy' section of this chapter.

**1.128** The government is also **investing £20 million to develop the Midlands Rail Hub**, progressing plans for a major programme of improvements to rail services across these regions.

### Local transport

**1.129** The government intends to make an unprecedented investment in urban transport, starting by **confirming allocations of over £1 billion from the Transforming Cities Fund.** This will deliver a range of local transport schemes, including an iconic new Central Park Bridge in Plymouth, a significant increase in the capacity of the Tyne and Wear Metro, and new cycleways in Bournemouth, Christchurch and Poole. In line with the government's priorities, this will also include around £800 million for bus and cycling infrastructure.

**1.130** Building on the Transforming Cities Fund, the government will also provide **£4.2 billion from 2022-23 for five-year funding settlements for eight Mayoral Combined Authorities** (in West Yorkshire, Greater Manchester, West Midlands, Liverpool City Region, Tyne and Wear, West of England, Sheffield City Region and Tees Valley). While it will be for elected Mayors to put forward ambitious plans, the government would welcome the opportunity to support a range of schemes, such as the renewal of the Sheffield Supertram, the development of a modern, low-carbon metro network for West Yorkshire and tram-train pilots in Greater Manchester. As a first step, the government will open discussions with Greater Manchester, Liverpool City Region and the West Midlands in the coming months.

[33] 'Departmental update', Department for Transport, October 2019.
[34] 'Lower Thames Crossing', Highways England.

**1.131** The government also intends to deliver better local transport for towns, rural areas and other cities. In February, the Prime Minister announced £5 billion of new funding for buses and cycling. Further details will be announced at the CSR, alongside a National Bus Strategy.

**1.132** Well-maintained roads are important for all road users, including cyclists and bus passengers. To that end, the Budget announces **a new Potholes Fund that will provide £500 million a year**, resulting in a 50% increase to local road maintenance budgets in 2020-21. Furthermore, the Budget confirms **the development of 15 local road upgrades across the country**, helping to reduce congestion, improve journey times and unlock housing and employment opportunities in England. These include junction improvements to the A350 in Wiltshire, a link road connecting Chesterfield to Staveley, and a dual carriageway in Warwickshire.

**1.133** The CSR will set out further plans for investment in local transport spending. To inform these plans, the Infrastructure and Projects Authority will lead a study, working with departments, into supply chain capacity, to assess how industry can best deliver the government's ambition.

## Digital connectivity

**1.134** Investment in broadband has had significant benefits to the UK economy.[35] Forty times faster than standard superfast broadband, gigabit broadband provides a step change in the UK's digital connectivity. The government is committing **£5 billion to support the rollout of gigabit-capable broadband in the most difficult to reach 20% of the country**, so that all areas are able to benefit. This investment will level up connectivity across the UK, particularly in rural areas.

**1.135** As part of over £1 billion that the government has already committed to next generation digital infrastructure, the Budget announces the **next seven areas that have successfully bid for funding from the third wave of the Local Full Fibre Networks Challenge Fund**: North of Tyne (£12 million), South Wales (£12 million), Tay Cities (£6.7 million), Pembrokeshire (£4 million), Plymouth (£3 million), Essex and Hertfordshire (£2.1 million) and East Riding of Yorkshire (£1 million).

**1.136** In too many places, phone reception is not good enough and people lack choice of mobile provider. **The Budget announces that the Shared Rural Network agreement has been finalised between the government and industry. The government will commit up to £510 million of funding, which will be more than matched by industry**. This means 95% of the UK's landmass will have high quality 4G mobile coverage by 2025.

## Flooding and water

**1.137** Flooding has a devastating impact on homes, businesses and communities, and the government is currently investing £2.6 billion in flood defences to ensure they are better protected. This winter, the Environment Agency's flood defences protected 127,000 properties.[36]

**1.138** However, the twin pressures of climate change and population growth mean that further action is needed. The government will **double the amount it invests in the flood and coastal defence programme in England to £5.2 billion over six years**, better protecting a further 336,000 homes and non-residential properties. According to Environment Agency modelling, this will reduce national flood risk by up to 11% by 2027. This doubling of funding

---

[35] 'The economic impact of broadband: evidence from OECD countries', Ofcom, April 2018.

[36] 'Flood risk begins to recede but public are warned to be vigilant', Environment Agency and Department for Environment, Food & Rural Affairs, February 2020.

exceeds the level of investment recommended by the National Infrastructure Commission. The government is also making available £120 million to the Environment Agency to **repair the assets** damaged by the storms this winter.

**1.139** Where flooding and coastal erosion is inevitable, further action is needed to ensure that communities can respond and recover more quickly. The government will provide £200 million over the next six years for a **place-based resilience programme**. This will support over 25 local areas, urban, rural and coastal, from the North, the Midlands and the South, to take forward wider innovative actions that improve their resilience to flooding and coastal erosion. Areas will be selected based on a range of criteria, including repeated significant flooding in the past.

**1.140** Climate change also makes it even more important that water resources are properly managed and conserved. The government will invest £39 million in the Environment Agency's network of **water supply and water navigation assets.**

**1.141** As floods do not respect national boundaries, it is right that the devolved administrations will benefit from the Barnett consequentials of this substantial increase in government investment in flood and water infrastructure.

## Housing

**1.142** Everyone should be able to access a safe and affordable home. Increasing housing supply is essential to creating a fairer, more affordable housing market and boosting productivity across the country.

**1.143** The government has made good progress in boosting housing supply with over 240,000 new homes created in 2018-19, the highest level in 32 years.[37,38] To continue to support the country's needs the government has committed to creating at least 1 million new homes in England by the end of this Parliament and an average of 300,000 homes a year by the mid-2020s.

**1.144** The Budget sets out an ambitious package of investment to build the high quality and affordable homes the country needs. This includes **£12.2 billion for the Affordable Homes Programme** and £400 million for ambitious Mayoral Combined Authorities and local areas to establish housing on brownfield land across the country. The Budget also confirms allocations from the Housing Infrastructure Fund totalling £1.1 billion for nine different areas including Manchester, South Sunderland and South Lancaster.

**1.145** Land availability, as constrained by the planning system, is the most significant barrier to building more houses. The Secretary of State for Housing, Communities and Local Government will shortly set out comprehensive reforms to bring the planning system into the 21st century, followed by a Planning White Paper in the spring. These reforms will aim to create a simpler planning system and improve the capacity, capability and performance of Local Planning Authorities (LPAs) to accelerate the development process. Where LPAs fail to meet their local housing need, there will be firm consequences, including a stricter approach taken to the release of land for development and greater government intervention. The government will also explore long-term reforms to the planning system, rethinking planning from first principles, to ensure the system is providing more certainty to the public, LPAs and developers.

[37] 'Written question – 292970', House of Commons, October 2019.

[38] 'Housing Statistical Release', Ministry of Housing, Communities & Local Government, December 2019.

## Skills

**1.146** Supporting people to improve their skills is a vital part of the government's aim to level up opportunity across the country. Increasing productivity depends on improving the skills levels of this generation and the next. Achieving this will require vocational and technical education that genuinely responds to the needs of business and the country as a whole. The government will confirm its plans on skills at the CSR. But the first steps come now.

**1.147** Further education should be at the forefront of providing all learners with the opportunity and tools to progress into skilled employment. At Spending Round 2019, the government increased day-to-day spending on further education by £400 million in 2020-21, recognising its vital role in equipping people with the skills they need to succeed.

**1.148** The Budget goes further, **providing £1.5 billion over 5 years (£1.8 billion inclusive of indicative Barnett consequentials) in capital investment to ensure that all further education college estates are in good condition**. This investment will ensure that colleges have cutting-edge facilities to train people for jobs in the industries of the future, and is part of the government's plan to upgrade the nation's infrastructure.

**1.149** Alongside this, adult skills provision must improve to meet the needs of people and business now and in the future. To address this issue, **the government has committed to a new £2.5 billion (£3 billion inclusive of indicative Barnett consequentials) National Skills Fund** to improve the technical skills of adults across the country.

**1.150** The government will consult widely in the spring on how to target this fund most effectively, before confirming details at the CSR. The government wants to hear directly from people and employers across England to understand what works in the current system and what does not, and to ensure that the fund is focused on helping people gain the skills they need for rewarding, well-paid jobs.

**1.151** More broadly, the government wants to facilitate two culture changes with this fund: for individuals to be able to train and retrain over the course of their lifetimes; and for employers and the government to increase investment and fill the skills gaps that hold back productivity at a local, regional and national level.

**1.152** Apprenticeships also provide the opportunity for people to learn valuable skills and get good jobs. Since its introduction in April 2017, the Apprenticeship Levy has enabled the government to raise the standard of apprenticeships, supporting employers to make a long-term, sustainable investment in training. The government will now look at how to improve the working of the Apprenticeship Levy, to support large and small employers in meeting the long-term skills needs of the economy. In the meantime, the government will ensure that sufficient funding is made available in 2020-21 to support an increase in the number of new high-quality apprenticeships in small- and medium-sized businesses.

## Growth across the country

**1.153** The growth of every region and nation in the UK is important for boosting the economy and creating a strong and inclusive society. In addition, the government will publish an English Devolution White Paper in the summer, setting out how it intends to meet its ambition for full devolution across England.

**1.154** Towns are home to some of our key businesses and employers. This is why the government has already set up the **£3.6 billion Towns Fund to support the regeneration of high streets, town centres and local economies**. The government is also supporting our ports, which are major hubs for trade, innovation and commerce – it has launched a consultation on creating up to 10 new Freeports that will work for all of the UK.

**1.155** The Budget goes further to support places, regions and nations to grow. As part of this **the government has agreed a devolution deal with West Yorkshire to establish a Mayoral Combined Authority with a directly-elected Mayor from May 2021**. This deal will provide £1.1 billion of investment for the area over 30 years, as well as devolving significant new decision-making powers on transport, planning and skills. It also underpins the agreement of a long-term intra-city transport settlement for the region starting in 2022-23. This devolution deal is an important step in delivering on our levelling up agenda by giving power and investment to local areas. As part of this, **the government is also providing up to £500,000 to support Bradford in its regeneration and development plans** to increase the benefits of potential Northern Powerhouse Rail connections.

**1.156** In repatriating the EU structural funds, the government has an historic opportunity to design a UK Shared Prosperity Fund to match domestic priorities. The UK Shared Prosperity Fund will replace the overly bureaucratic EU structural funds, levelling up opportunity in each of the four nations of the country. Funding will be realigned to match domestic priorities, not the EU's, with a focus on investing in people. At a minimum, it will match current levels of funding for each nation from EU structural funds. The government will set out further plans for the Fund, including at the CSR.

**1.157** The Budget also sets out how the government will make decisions differently in future. To ensure the civil service reflects the public it serves, **the government is committed to moving 22,000 civil service roles out of central London within the next decade**, the vast majority to the other regions and nations of the UK. The government will **establish a significant new campus in the north of England** focused on economic decision making, which will include teams from HM Treasury, DIT, BEIS and MHCLG. **Furthermore, as the UK's economics and finance ministry HM Treasury will establish representation in all the nations of the UK**, building on its existing presence in Scotland with new positions based in Northern Ireland and Wales for the first time.

**1.158** A cornerstone of the government's levelling up agenda is its commitment to regional connectivity. The aviation industry has an important role to play in connecting the nations and regions of the UK. Following the review of Air Passenger Duty (APD) that has been undertaken by HM Treasury, the government will consider the case for changing the APD treatment of domestic flights, such as reintroducing a return leg exemption, and for increasing the number of international distance bands. These considerations will form part of a **consultation on aviation tax reform** that will be published in spring 2020.

## Scotland, Wales and Northern Ireland

**1.159** As part of its commitment to levelling up the whole of the UK, the government will support economic growth in each of the four nations and will strengthen the ties that bind them into a prosperous United Kingdom. The government will work closely with the devolved administrations on this agenda, especially where it is possible to achieve better outcomes in partnership with Cardiff Bay, Holyrood and Stormont.

**1.160** The Budget announces changes across tax, welfare and public spending that apply across the whole of the UK and so will directly benefit people and businesses in Scotland, Wales and Northern Ireland. This includes steps to upgrade digital infrastructure, support decarbonisation and reduce tax for employees and the self-employed.

**1.161** Where Budget measures do not apply across all nations, **the devolved administrations will receive significant additional funding through the Barnett formula** to invest further in public services, infrastructure and other priorities:

- the Scottish Government's block grant will increase by over £640 million through to 2020-21 before adjustments for tax devolution
- the Welsh Government's block grant will increase by over £360 million through to 2020-21 before adjustments for tax devolution, this includes a 5% uplift in Barnett consequentials agreed as part of the Welsh Government's fiscal framework in 2016
- the Northern Ireland Executive's block grant will increase by over £210 million through to 2020-21

**1.162** The Budget announces £242 million to fund a further four City and Growth Deals across Scotland, Wales and Nothern Ireland. This builds on the £2.5 billion already allocated to existing deals and ensures that every part of Wales and Nothern Ireland benefits from a City or Growth Deal, with another deal that benefits Scotland.

**1.163** The government will also take action to improve cross-border links, including improving transport links between North Wales and England by developing the A483 Pant Llanymynech Bypass, and supporting an independent economic review of the Western Gateway, which stretches across Wales and the west of England.

**1.164** The Budget announces further support targeted at each of the nations – including a package for the whisky industry, action to allow TV channel S4C to recover in full any VAT it pays, and legislation to provide appropriate exemptions for payments for injuries relating to the Troubles in Northern Ireland.

**1.165** Additionally, the government is working with the Scottish Government to devolve further tax and welfare powers as set out in the Scotland Act 2016. This includes transferring responsibility to the Scottish Government for around £3 billion of disability benefits in April 2020 and, from 2021, assigning half of the VAT revenues generated in Scotland.

**1.166** Further details and additional announcements targeted at levelling up and getting Britain building can be found in Chapter 2.

# Supporting people and families

**1.167** Record employment and rising real wages have benefited households across the country.[39] The OBR forecasts employment to rise by 522,000 by the first quarter of 2025 and wages to outpace inflation in every year of the forecast.[40] The government's ambition is to support people and families through a fair and sustainable tax system, that rewards hard work, minimises economic distortions and funds first class public services.

**1.168** The Budget announces a range of measures to improve living standards for people across the UK, delivering on commitments to cut taxes and costs, to put more money in people's pockets.

## Helping hard-working people

**1.169** The government is committed to keeping taxes low, helping hard-working people keep more of what they earn. In less than a decade, the Personal Allowance has increased by over 90% and has taken 1.7 million individuals out of income tax altogether compared to 2015-16.[41,42] The Budget confirms the government's commitment to **increase the National Insurance contributions (NICs) Primary Threshold and Lower Profits Limit, for employees and the self-employed respectively, to £9,500 from April 2020**.[43] (12)

**1.170** This increase will benefit around 31 million people,[44] with a typical employee saving around £104 and a typical self-employed person around £78 in 2020-21.[45] Around 1.1 million people will be taken out of paying Class 1 and Class 4 NICs entirely.[46] This is the first step in meeting the government's ambition to increase these thresholds to £12,500, which would save a typical employee over £450 per year.[47] Taken together with increases to the National Living Wage (NLW) and previous increases to the Personal Allowance, an employee working full-time on the NLW anywhere in the UK will be over £5,200 better off compared to April 2010.[48] This reform is in line with the government's ambition to support hardworking people and families through a fair and sustainable tax system.

**1.171** By saving towards their future, families can give children a significant financial asset when they reach adulthood – helping them into further education, training, or work. Junior ISAs (JISAs) and Child Trust Funds (CTFs) are tax-advantaged accounts for children, designed to encourage a long-term savings habit. The Budget announces that **the amount families can save into a JISA or CTF will be more than doubled in 2020-21, increasing from £4,368 to £9,000**.

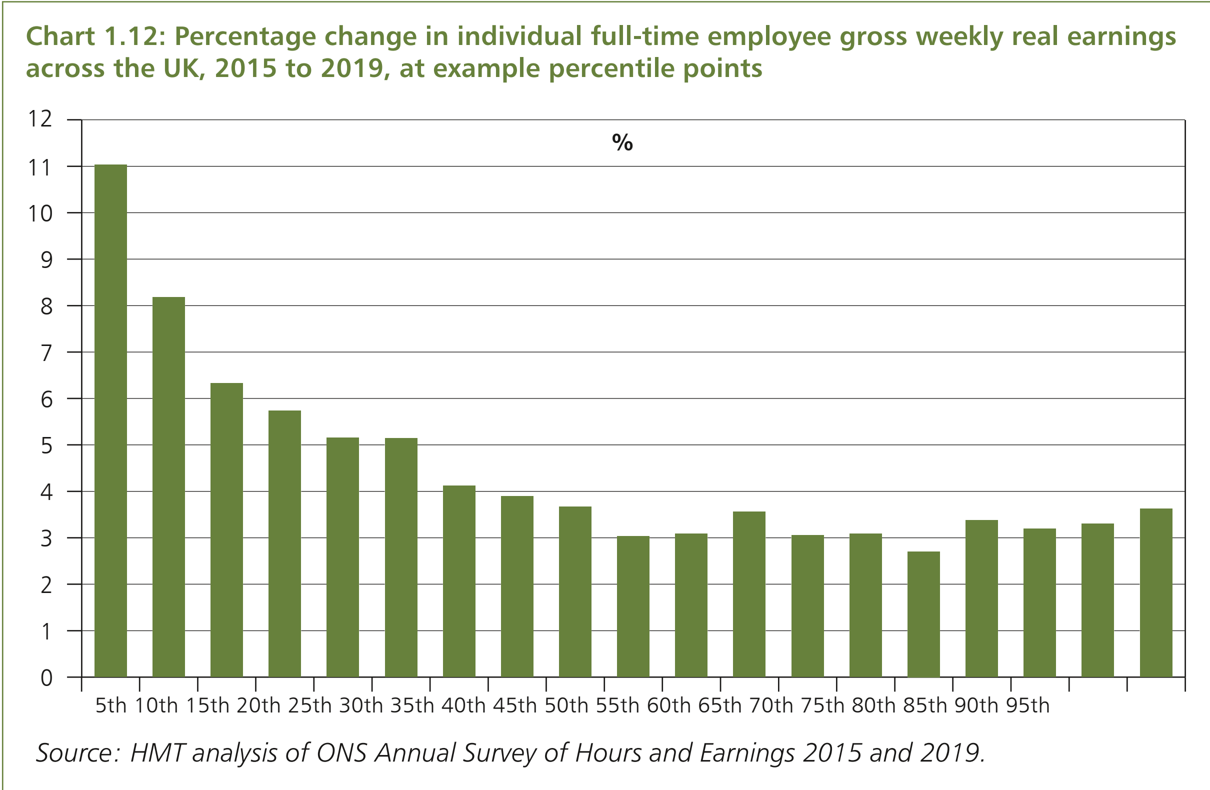
## Fairer wages for the lowest paid

**1.172** Since its introduction in 2016, the NLW has supported rapid earnings growth for the lowest earners. Supported by the NLW, real wages have grown fastest for the lowest paid full–time workers, by 11% above inflation between 2015 and 2019.[49] Following the recommendations of the Low Pay Commission (LPC), the government announced in December

[39] See 'Budget 2020 data sources'.
[40] 'Economic and Fiscal Outlook', OBR, March 2020.
[41] HMRC analysis based on Survey of Personal Incomes (SPI) 2017-18 data, and Budget 2020 OBR forecast.
[42] Up to the year 2019-20.
[43] '31 million taxpayers to get April tax cut', HM Treasury, 30 January 2020.
[44] HMRC analysis based on Survey of Personal Incomes (SPI) 2017-18 data, and Budget 2020 OBR forecast.
[45] HM Treasury analysis, see 'Budget 2020 data sources'.
[46] HMRC analysis based on Survey of Personal Incomes (SPI) 2017-18 data, and Budget 2020 OBR forecast.
[47] HM Treasury analysis, see 'Budget 2020 data sources'.
[48] HM Treasury analysis, see 'Budget 2020 data sources'.
[49] HM Treasury analysis of ONS Annual Survey of Hours and Earnings, 2015 results and 2019 results. 'Lowest–paid full–time workers' defined as those at the fifth percentile of the earnings distribution.

2019 that it will **increase the NLW by 6.2% from £8.21 to £8.72 from April 2020,** which is projected to meet its current target of 60% of median earnings by 2020.[50] In total, the annual gross earnings of a full-time worker on the NLW will have increased by over £3,680 since the introduction of the NLW in April 2016.

**Chart 1.12: Percentage change in individual full-time employee gross weekly real earnings across the UK, 2015 to 2019, at example percentile points**




*Source: HMT analysis of ONS Annual Survey of Hours and Earnings 2015 and 2019.*

**1.173** The Budget commits to **a new, ambitious target for the NLW to reach two-thirds of median earnings and extending this to workers aged 21 and over by 2024**, provided economic conditions allow. This emergency brake will ensure that the lowest-paid workers across the UK continue to see pay rises without significant risks to their employment prospects.

## Cutting the cost of living

**1.174** The government will introduce legislation to **apply a zero rate of VAT to e-publications** from 1 December 2020, which will make it clear that e-books, e-newspapers, e-magazines and academic e-journals are entitled to the same VAT treatment as their physical counterparts. The government expects the publishing industry, including e-booksellers, to pass on the benefit of this relief to consumers. It should benefit all who read digitally, including children from poorer backgrounds: nearly 1 in 4 pupils on free school meals read fiction digitally, compared to 1 in 6 of their peers who are not eligible for free school meals.[51]

**1.175** In recognition of the rising cost of living, the government will **freeze fuel duty for a record tenth year in a row, saving the average car driver a cumulative £1,200 compared to what they would have paid under the pre-2010 fuel duty escalator.**[52] (13)

**1.176** Now that the UK has left the EU, it can reduce the cost of essential sanitary products for women in the UK. From 1 January 2021, **the tampon tax will be abolished through the application of a zero rate of VAT on women's sanitary products.** (17)

[50] www.gov.uk/national-minimum-wage-rates.
[51] 'Children, young people and digital reading', National Literacy Trust, April 2019.
[52] HM Treasury calculations.

**1.177** The Budget also announces that the government will **freeze duty rates on beer, spirits, wine and cider**, meaning that a pint of beer is 1p cheaper than it would have been if it had risen with inflation.

**1.178** The government is announcing a **service improvement that will make Tax-Free Childcare (TFC) compatible with school payment agents**. This will allow parents of up to 500,000 school-aged children across the UK to access TFC and use it towards the cost of their wraparound childcare. (14)

**1.179** Recognising housing costs are the biggest pressure on household finances for low income households, these measures go alongside other substantial new packages of support to **increase housebuilding and improve the affordability of housing,** as detailed in Levelling Up and getting Britain building.[53]

## Supporting the most vulnerable

**1.180** The government is delivering on its commitments to provide a clear route to work and support the most vulnerable through the welfare system. This government is ending the benefit freeze and **increasing working age benefits by 1.7% from April 2020.** Providing further support for Universal Credit (UC), the government will help ensure claimants can repay debts in a more sustainable and manageable way by **reducing the maximum rate at which deductions can be made from a UC award from 30% to 25% of the standard allowance and giving claimants up to 24 months to repay advances.**

**1.181** The government will give people with disabilities greater certainty over their award levels for longer, by guaranteeing that **Personal Independence Payment claimants will not have an award period of less than 18 months**. (19)

**1.182** The government will create an **entitlement to Neonatal Leave and Pay** for employees whose babies spend an extended period of time in neonatal care, providing up to 12 weeks paid leave so that parents do not have to choose between returning to work and taking care of their vulnerable newborn. In addition, the government will **consult on the design of a new in-work entitlement for employees with unpaid caring responsibilities**, such as for a family member of dependents. (20)

**1.183** The government is committed to helping people in problem debt and, from early 2021, will introduce breathing space. This will provide a period of up to 60 days, where people in problem debt will be protected from enforcement action by their creditors and the charging of further interest and fees on their debts. This includes debts owed to central and local government. To support that, the government will invest an **additional £12.5 million in HMRC in 2020-21 to begin work immediately on the implementation of breathing space**.

**1.184** The government will commit **£46 million from the Shared Outcomes Fund to provide improved support to individuals overcoming multiple complex needs,** such as homelessness, reoffending and substance misuse.

**1.185** Following the Grenfell tragedy, one of the government's most important objectives is to ensure residents feel safe and secure in their home. Having taken expert advice, the Budget confirms an **additional £1 billion to remove unsafe cladding from residential buildings above 18 metres to ensure people feel safe in their homes.**

[53] HM Treasury analysis, see 'Budget 2020 data sources'.

**1.186** The government wants to support alternatives to high-cost credit such as payday loans, particularly for the most financially vulnerable consumers, by improving access to social and community lenders. The Budget announces the **three winners of the £2 million Affordable Credit Challenge Fund**, which is designed to harness the UK's world-leading fintech expertise to develop tech solutions to the challenges faced by the affordable lending sector, making it easier and quicker to access their products.

**1.187** The Budget also announces that the government will **provide protection against misleading sales tactics for consumers who are planning for their funeral,** ensuring that all pre-paid funeral plan providers are subject to robust regulation by bringing the market within the remit of the FCA.

**1.188** The Budget announces that the government will bring forward **legislation to protect access to cash** and ensure that the UK's cash infrastructure is sustainable in the long-term.

## Rough Sleeping

**1.189** The government is committed to ending rough sleeping in this Parliament. Government action is already having an impact, with the latest annual count for England published in February showing a 9% fall on the previous year.[54] The Budget seeks to build on this progress with £643 million for accommodation and support services to help people off the streets and to start rebuilding their lives. Money raised from a 2% non-UK resident Stamp Duty Land Tax surcharge will be used to help fund policies to reduce rough sleeping in England. (22, 47)

**1.190** The government is introducing **additional exemptions from the Shared Accommodation Rate (SAR) for Universal Credit and Housing Benefit claimants** to protect those at risk of homelessness. This will enable rough sleepers aged 16-24, care leavers up to the age of 25, and victims of domestic abuse and human trafficking to live on their own, supporting their recovery from homelessness. (21)

**1.191** Further details and additional announcements targeted at supporting people and families can be found in Chapter 2.

[54] Rough sleeping snapshot in England: autumn 2019, Ministry of Housing, Communities & Local Government, February 2020.

# Backing business

**1.192** Businesses provide the jobs that hard-working families depend on today, and through investment and innovation they will create the jobs of tomorrow. Backing business is vital to levelling up the economy across the regions and nations of the UK and boosting productivity growth.

**1.193** The government is committed to making the UK the best place to start and grow a business, supporting enterprising businesses to succeed while attracting established businesses to locate and invest in the UK. In order to do so, the government is investing in the priorities of the business community by improving transport networks and digital connectivity and by investing in people's skills and health. The government will ensure that the UK's tax system remains competitive and that the regulatory regime supports competition and innovation, along with improving business support and ensuring the UK becomes a 21st century exporting superpower.

## Business and enterprise support

**1.194** Supporting enterprise is an important part of the government's ambition to level up opportunity across the UK. The government will do this directly by **extending the funding of the British Business Bank's Start-Up Loans programme to the end of 2021-22**, supporting up to 10,000 further entrepreneurs across the UK to access finance to start a business.

**1.195** To ensure that all businesses have access to high quality support and advice in their region, the government will **invest £10 million to increase Growth Hub capacity** and provide high-quality, core business advice and guidance across all 38 Growth Hubs.

**1.196** In addition, the government will **invest £13 million to expand the British Library's network of Business and Intellectual Property Centres** to 21 cities and 18 surrounding local library networks across England, providing entrepreneurs with business support, free access to market intelligence, IP workshops and one-to-one coaching. (29)

**1.197** The government will use the forthcoming CSR to make it easier for businesses to access the information and support that is relevant for them. As a first step, BEIS will **lead the development of a digital service to provide businesses with tailored information about appropriate sources of support.**

**1.198** The UK is a global financial centre, with world-leading finance hubs in London, Edinburgh, Birmingham and Leeds that support jobs across the country. To maintain the competitiveness of the UK financial services sector, the government will be taking a number of steps to ensure that the UK's regulatory regime remains proportionate and effective. These will enhance coordination between regulators and ensure the UK continues to lead the way on financial services innovation and the use of technology, including on the regulation of payments and cryptocurrencies. The government will also introduce a Financial Services Bill later in the session which will ensure that the UK maintains its world-leading regulatory standards and remains open to international markets.

## Support for the self-employed

**1.199** The government has reviewed how support for the self-employed can be strengthened. It will improve access to finance and credit for self-employed people, by extending funding for the Start-Up Loans programme as above and by **exploring how to improve the guidance available for self-employed people applying for a mortgage.** Self-employed people

will also benefit from the government's continued efforts to tackle late payments. BEIS will shortly **publish a consultation on the merits of strengthening the powers of the Small Business Commissioner.**

**1.200** The government will make it easier for self-employed people to find the information and guidance that is relevant to them and their business. The Budget announces that HMRC will **launch new interactive guidance in summer 2020 which will make it easier for self-employed taxpayers to navigate the tax system.** They will also benefit from the new digital support service described above. Self-employed people working in rural and hard to reach areas will benefit from the £5 billion for gigabit-capable broadband rollout and funding to improve mobile coverage that the Budget announces.

**1.201** Additionally, the government will **consider how to provide appropriate support to self-employed parents** so that they can continue to run their businesses, as part of its wider review of Parental Pay and Leave.

## Competition and regulation

**1.202** Competition is essential to drive innovation, produce better outcomes for consumers and allow new entrants to the market to grow. The UK is at the forefront of designing smarter and more flexible regulation that allows competition to flourish and minimises unnecessary burdens for business.

**1.203** To empower consumers and boost competition, the government will **accept all six of the Furman Review's[55] strategic recommendations** for unlocking competition in digital markets.

**1.204** To reduce regulatory barriers for businesses and ensure that regulation is sensible and proportionate now that the UK has left the EU, the Budget launches the **Reforming Regulation Initiative** to invite ideas from business and the public for regulatory reform. Boosting regulators' capacity is also essential to unlock the potential of emerging technologies and help businesses to develop innovative products and services, and the Budget announces that the government will invest **£10 million in a second round of the Regulators' Pioneer Fund**.

**1.205** The government intends to **introduce a levy to be paid by firms subject to the Money Laundering Regulations to help fund new government action to tackle money laundering** and ensure delivery of the reforms committed to in the Economic Crime Plan. These reforms will help safeguard the UK's global reputation as a safe and transparent place to conduct business. The levy will be additional to ongoing public sector funding. The government will publish a consultation on the levy later this spring.

## Global Britain

**1.206** The UK is an outward-looking and open economy. The government is implementing an independent trade policy for the first time in over 40 years, continuing to support businesses seeking to export and encouraging investors to choose the UK. The Budget takes further steps to enhance this support for trade and investment.

**1.207** To strengthen the global ties of our digital technology sector, DIT and the Department for Digital, Culture, Media and Sport (DCMS) will **pilot a Digital Trade Network in the Asia Pacific region**, helping innovative UK companies to access opportunities in major new markets.

[55] 'Unlocking digital competition, Report of the Digital Competition Expert panel', HM Treasury, March 2019.

DIT will establish **local champions based at key overseas posts to support exporters from the Northern Powerhouse, Midlands Engine, and Western Gateway,** and will **increase the number of international trade advisers outside London.**

**1.208** The Budget also announces further support for exporters by **extending and increasing the lending capacity of UK Export Finance (UKEF)**. This will make permanent the additional £2 billion provided to UKEF at Budget 2018 as well as provide a new £2 billion lending facility for projects supporting clean growth and a new £1 billion to support overseas buyers of UK defence and security goods and services. UKEF will also expand its face-to-face support for exporters focused on clean growth in the North of England and Scotland where energy supply chains are economically important.

**1.209** The government will support the UK's world-leading fintech sector, along with the wider digital economy. The Budget announces a **review of the UK fintech sector led by Ron Kalifa OBE to support growth and competitiveness in the sector**. In addition, the government will **convene a summit looking at what further data needs to be made accessible to make it faster and easier for SMEs to shop around for credit.**

## A competitive tax environment

**1.210** The government will maintain a sustainable and efficient business-friendly tax environment in which innovative and enterprising businesses can grow and thrive.

**1.211** By confirming that the headline **corporation tax rate will remain at 19% in 2020**, the lowest in the G20,[56] the Budget ensures that the UK will continue to be an attractive place to do business while allowing the government to take action to address the most important challenges businesses face and increase funding for infrastructure and vital public services. An **increase in the annual rate of the structures and buildings allowance to 3%** will provide over £1 billion in additional relief for businesses by the end of 2024-25. Together with measures to incentivise spending on R&D, this will unlock new investment and further enhance the international competitiveness of the UK tax system. The Budget also announces **reforms to the intangible fixed assets regime** to reinforce the attractiveness of the UK as a place for businesses to own and manage intellectual property, **a review of the UK funds regime**, as well as **an industry working group on the future of VAT and financial services**. (45, 23, 28)

**1.212** Small businesses play a crucial role in driving the economy and creating jobs. The government will help small businesses take on extra staff to fulfil their potential and boost employment by delivering on its commitment to **increase the Employment Allowance to £4,000**. As a result, businesses will be able to employ four full-time employees on the National Living Wage without paying any employer National Insurance contributions (NICs). This measure will benefit around 510,000 businesses, including around 65,000 businesses which will be taken out of paying NICs entirely.[57] From April, over 650,000 businesses will have been taken out of paying NICs since the introduction of the Employment Allowance in 2014.[58] The government will also meet its commitment to **introduce a National Insurance holiday for employers of veterans** in their first year of civilian employment. (25,16)

**1.213** The government will continue to use the tax system to support genuine risk-taking and creativity where it is proven to be effective. In response to evidence that Entrepreneurs' Relief has primarily benefited a small number of very affluent taxpayers and done little to generate additional entrepreneurial activity,[59] the government will **reduce the lifetime limit on gains**

[56] 'Corporate tax rate table', KPMG, 2019.

[57] HMRC analysis based on Pay As You Earn Real Time Information, the ONS Inter-Departmental Business Register.

[58] ibid.

[59] 'Capital Gains Tax Entrepreneur's Relief: Behaviours and Motivations' IFF Research, May 2017.

**eligible for relief to £1 million**. This will ensure that enterprising small business owners will continue to benefit, leaving over 80% of those using the relief unaffected,[60] while making the tax system fairer and more sustainable. (46)

**1.214** The government is committed to supporting businesses which form an important part of our communities and high streets. The Budget confirms that the government will support shops, pubs, cinemas, and music venues in England by **increasing and expanding the business rates discount for retail properties, introducing a new pubs discount**, and **extending the local newspaper discount**. To support businesses affected by COVID-19, the government has gone further than previously announced, as detailed earlier in the chapter. A **fundamental review of business rates** will consider further reforms to the business rates system and will report in the autumn. (26, 27)

**1.215** The government wants to make the most of the opportunity of leaving the EU to make our VAT and excise system more business-friendly, while continuing to recognise the significant contribution of VAT and excise towards the public finances. The Budget meets the government's commitment to **review the alcohol duty regime** to ensure it works for UK producers and consumers. **Postponed VAT accounting** will also change the time when import VAT is due to HMRC, providing an important cash flow advantage to businesses across the country that are integrated in international supply chains as they adapt to the UK's position as an independent trading nation.

**1.216** The Budget announces a set of targeted measures to ensure that businesses pay the tax they owe, ensuring fairness for everyone. This includes **measures to crack down on tax abuse in the construction industry, illicit tobacco**, and **among big business**, as well as **measures to tackle the promoters of tax avoidance schemes**. (57)

**1.217** Further details on how the government is backing business can be found in Chapter 2.

[60] Internal HMRC analysis of Entrepreneur's Relief data.

# Investing in innovation

**1.218** The UK has a long and rich history as a hub for scientific discovery and transformative technological progress. From the foundations of scientific investigation and the development of the laws of motion, through the industrial revolution and into the modern digital age – for centuries the UK has led the world. With less than 1% of the world's population, the UK hosts 4 of the world's 20 best universities,[61] has produced up to 14% of the world's most impactful research[62] and has the second highest number of Nobel Laureates of any nation.[63] Today, UK researchers and businesses are cutting carbon emissions, curing genetic diseases and pushing the frontier of artificial intelligence. The UK is also home to some of the world's foremost technology-pioneering businesses, and UK research attracts significant foreign direct investment.

**1.219** Research and innovation lead to better products, services and processes. These drive growth and prosperity across the country, and generate ideas and tools to tackle global challenges such as climate change and an ageing population. That is why the government set the objective of increasing economy-wide investment in R&D to 2.4% of GDP by 2027, and why the Budget puts science, innovation and technology at the heart of the UK's investment strategy.

**1.220** The Budget sets out ambitious plans to **increase public R&D investment to £22 billion per year by 2024-25.** This landmark investment is the largest and fastest ever expansion of support for basic research and innovation, taking direct support for R&D to 0.8% of GDP and placing the UK among the top quarter of OECD nations – ahead of the USA, Japan, France and China.[64] This unprecedented increase in investment will support a range of objectives, including:

- supporting world-leading research in all regions and nations of the UK, including by **cutting bureaucracy, experimenting with new funding models, and establishing a new funding agency to focus on high-risk, high-reward research**
- meeting the great challenges facing society, including climate change and an ageing population, and **providing funding to pursue 'moonshot' scientific missions**
- **investing in the government's own strategic science capability and improving public services**
- **backing businesses to invest and innovate** so that they can compete in the global technology-driven economy

**1.221** Details of how this funding will support these and other objectives will be set out at the forthcoming CSR, but the Budget announces a set of measures that will have an immediate impact.

## Supporting world-leading research in all regions and nations

**1.222** The UK has excellent universities in every region and nation that attract business investment, deepen the skills and knowledge of the population, and drive economic growth. The government is **providing an immediate funding boost of up to £400 million in 2020-21 for world-leading research, infrastructure and equipment**. This will help build excellence in research institutes and universities right across the UK, particularly in basic research and physical sciences. The government will also provide **£300 million for experimental**

[61] Times Higher Education World University Rankings 2020.
[62] 'International Comparison of the UK research base, 2019', Department of Business, Energy and Industrial Strategy, July 2019.
[63] USA is 1st with 368, followed by the UK with 132. Source: Nobelprize.org
[64] Based on most recent available OECD Data: Main Science and Technology Indicators.

**mathematical research to attract the very best global talent** over the next five years. This will double funding for new PhDs and boost the number of maths fellowships and research projects.

**1.223** In addition, the government will **invest at least £800 million in a new blue-skies funding agency here in the UK,** modelled on the extraordinary 'ARPA' in the US.[65] This agency will fund high-risk, high-reward science.

**1.224** In recognition of their excellence and global reach, the government will **increase funding for the UK's foremost specialist institutions by £80 million over the next five years**. This will support world-leading organisations such as the London School of Hygiene and Tropical Medicine, the Royal College of Art and the Institute of Cancer Research among others. At the CSR, the government will **examine how R&D funding as a whole can best be distributed** across the country to help level up every region and nation of the country.

## Overcoming societal challenges

**1.225** The UK is a world leader in many of the scientific fields that are essential for responding to society's greatest challenges. For example, 25 of the world's top 100 medicines were discovered in the UK,[66] and the UK is the second largest expert contributor to the Intergovernmental Panel on Climate Change (IPCC).[67] The Budget is backing UK scientists and businesses to maintain and build on this international leadership.

**1.226** As part of this, to help meet the challenge of net zero and ensure that the UK is at the forefront of new decarbonisation technologies, the Budget commits to **at least double the size of the Energy Innovation Programme.**

**1.227** The government is also committed to deepening understanding of how to reduce the burden of illness in the future. To this end, the government is **committing an extra £12 million for the National Institute for Health Research in 2020-21**. This increased investment will target research into preventable diseases to work towards solving a range of major health challenges.

## Invest in government science capabilities and public science estate

**1.228** Cutting-edge science and innovation can also help the government to ensure that it is sufficiently equipped to foresee challenges and opportunities and improve public services. The government will therefore **invest £2 million in 2020-21 to expand the cross-cutting strategic science and resilience capabilities provided by the Government Chief Scientific Adviser and the Government Office for Science**. Furthermore, by **investing £1.4 billion over 10 years in the animal health science facility at Weybridge**, the government will enhance this world-class capability, underpinning agricultural trade and protecting the UK from the increasing threats of current and emerging animal diseases.

**1.229** In recognition of its global scientific significance, the Budget **provides £180 million over 6 years for a new state-of-the-art storage and research facility for the Natural History Museum** at Harwell Science and Innovation Campus. This upgrade will put the facility at the forefront of natural sciences research and international collaboration, housing and increasing access to around 40% of this world-leading biological collection.

---

[65] Advanced Research Projects Agency.

[66] BMI Research (2016) United Kingdom Pharmaceuticals & Healthcare Report Q1 2016, p61.

[67] Royal Society, "Investing in UK R&D", pg.2. Calculated from the annex of author and expert reviewers in the IPCC's Fifth Assessment Report.

## Backing businesses to innovate and grow

**1.230** Private investment will be crucial to meeting the government's objective of increasing economy-wide investment in R&D to 2.4% of GDP by 2027, and to creating an innovation-intensive and technology-driven economy. The Budget will support and encourage this by **increasing the rate of Research & Development Expenditure Credit from 12% to 13%**. The government will also **consult on whether qualifying R&D tax credit costs should include investments in data and cloud computing**. (24)

**1.231** The government is committed to ensuring that the UK's fast-growing and innovative businesses continue to have access to the finance they need to invest and grow. **The Life Sciences Investment Programme will provide the British Business Bank with additional resources to make up to £200 million in equity commitments** to support the UK's most innovative health and life sciences firms over the next five years. Invested alongside private sector capital, this is expected to enable £600 million of finance to create high-quality jobs and help UK patients benefit from more ground-breaking treatments and care. This funding will build on the £350 million of finance to life sciences firms currently supported by the British Business Bank by supporting large-scale venture growth funds. The programme will launch within a year. The government will **also provide the British Business Bank with the resources to make up to £200 million of additional investment in UK venture capital and growth finance in 2020-21.**

**1.232** The Budget will also **invest over £900 million to ensure UK businesses are leading the way in high-potential technologies**. This will involve commercialising nuclear fusion technology, offering potentially limitless clean energy, and supporting the government's ambitious National Space Strategy and space innovation fund. A portion of this funding contributes to a wider investment of up to £1 billion to develop UK supply chains for the large-scale production of electric vehicles, as announced in September.

**1.233** Further details on the support offered in the Budget for innovation can be found in Chapter 2.

# Growing a greener economy

**1.234** Reducing carbon emissions and enhancing the environment are major government priorities. The UK is already a leader in climate change and clean growth, having reduced emissions faster than any other G7 nation since 1990,[68] and being the first major economy to legislate for net zero greenhouse gas emissions.

**1.235** This year, as the UK prepares to host the COP26 Climate Summit,[69] the government is raising its ambition to decarbonise the economy. This will level up green economic opportunities in every nation and region and boost innovation, whilst also improving the natural environment.

**1.236** The Budget sets out ambitious action on tree planting, ultra-low emission vehicles, heat decarbonisation and carbon capture and storage. Further climate policy measures will follow in the coming months.

**1.237** HM Treasury will also publish two reviews this year – one into the economic costs and opportunities of reaching net zero, the other led by Professor Sir Partha Dasgupta into the economics of biodiversity.

## Decarbonising power, industry and heat

**1.238** Research and innovation will reduce the costs of meeting net zero and put the UK at the forefront of the new technologies needed to decarbonise the world economy. The Budget therefore commits to at least **doubling the size of the Energy Innovation Programme**. But innovation alone is not enough. Whilst new technologies are being developed, the government will continue to take action to reduce emissions now.

**1.239** The government has already made significant progress in reducing carbon emissions from electricity generation, driven by the switch from coal to gas and the growth in renewable energy. Costs have fallen so quickly that offshore wind, onshore wind and solar are likely to be the UK's primary source of electricity in the future. However, the power generated by these renewable sources is dependent on the weather, so the UK also needs reliable low carbon power from technologies such as nuclear, gas with carbon capture and storage (CCS), and hydrogen.

**1.240** To meet the net zero target, the UK must also decarbonise industry. There are a number of possible routes – from using low carbon energy sources like hydrogen or electricity, to capturing industrial emissions and storing them safely under the ground. This challenge provides opportunities not only to reduce emissions, but also to enable our manufacturing heartlands to become leaders in the green markets of the future.

**1.241** Carbon capture and storage will be important to decarbonising both power and industry. It can provide flexible low carbon power and decarbonise many industrial processes, whilst also offering the option for negative emissions at scale. The Budget announces a **CCS Infrastructure Fund to establish CCS in at least two UK sites,** one by the mid-2020s, a second by 2030. Using consumer subsidies, the government will also support the construction of the **UK's first CCS power plant.**

**1.242** The heating of our homes will need to be virtually zero carbon by 2050, replacing natural gas and other fossil fuels with low carbon alternatives – likely to be primarily a mix of green gas, heat pumps and heat networks. To meet this challenge, the Budget accelerates the greening of the gas grid by announcing **a new support scheme for biomethane**, funded by a **Green Gas Levy**. The government will also support the installation of heat pumps and biomass boilers by introducing a **Low Carbon Heat Support Scheme**. Recognising the energy

[68] 'Reducing UK emissions: 2018 Progress Report to Parliament', Committee on Climate Change, June 2018.
[69] 26th Conference of the Parties to the United Nations Framework Convention on Climate Change.

efficiency benefits of heat networks, the Budget **confirms funding for the Heat Networks Investment Project** for a further year to 2022 and provides **£270 million of new funding** to enable new and existing heat networks to adopt low carbon heat sources.

**1.243** To encourage businesses to operate in a more environmentally friendly way, the government is **raising the Climate Change Levy on gas in 2022-23 and 2023-24** (whilst freezing the rate on electricity) and **reopening and extending the Climate Change Agreement scheme** by two years. (40, 41)

## Reducing vehicle pollution

**1.244** Meeting the UK's net zero commitment will require emissions reductions across all modes of transport. However, road transport is responsible for 91% of domestic transport greenhouse gas emissions[70] and is one of the biggest contributors to poor air quality in the UK's towns and cities. The government has set ambitious targets to increase the number of zero emission vehicles on the road and is currently consulting on bringing forward the phaseout date for the sale of new petrol and diesel cars and vans from 2040. Meeting these targets will require a combination of spending, regulation and taxes.

**1.245** Consumer incentives support the development of markets for new transport technology. The government is considering the long-term future of incentives for zero emission vehicles alongside the 2040 phase-out date consultation. Until then, the government will provide **£403 million for the Plug-in Car Grant**, extending it to 2022-23. Recognising that the market for other ultra-low emission vehicles is still very small, the government will also **provide £129.5 million to extend the Plug-in Grants for vans, taxis and motorcycles to 2022-23.** In addition, the Budget announces the **exemption of zero emission cars from the Vehicle Excise Duty (VED) 'expensive car supplement'** and the publication of a call for evidence on VED, which will include how it can be further used to reduce vehicle emissions. (35, 44)

**1.246** Access to high quality, convenient charging infrastructure is critical for drivers to make the switch to electric vehicles confidently. The government is therefore **providing £500 million over the next five years to support the rollout of a fast-charging network for electric vehicles**, ensuring that drivers will never be further than 30 miles from a rapid charging station. This will include a **Rapid Charging Fund** to help businesses with the cost of connecting fast charge points to the electricity grid. To target spending from this fund effectively, the Office for Low Emission Vehicles will complete a **comprehensive electric vehicle charging infrastructure review**.

**1.247** The government will also **remove the entitlement to use red diesel from April 2022**, except in agriculture, fish farming, rail and for non-commercial heating (including domestic heating). By removing this tax relief on pollution, the government will encourage businesses and industry to improve the energy efficiency of their vehicles and machinery or look for greener alternatives. The development of these alternatives will be supported by the government more than doubling its investment in the Energy Innovation Programme. (39)

**1.248** Cleaner vehicles will improve air quality. The government is committed to bringing roadside concentrations of polluting nitrogen dioxide gas within legal limits in the shortest possible time. The Budget therefore allocates an additional **£304 million to enable local authorities to take immediate steps to reduce nitrogen dioxide emissions**. This brings the total amount that government has provided to affected local authorities to £880 million, meeting the government's obligations to all affected local authorities. (36)

[70] 'Transport Statistics Great Britain 2019', Department for Transport, December 2019.

## Natural environment

**1.249** This government aims to be the first to leave the natural environment in a better condition than we inherited it. The '25 Year Environment Plan' sets out the government's ambitions for clean air and water, thriving plants and wildlife, and mitigating and adapting to climate change.[71]

**1.250** The Budget announces the **Nature for Climate Fund** which will **invest £640 million in tree planting and peatland restoration** in England, increasing the rate of tree planting by over 600%[72] and covering an area greater than Birmingham over the next five years. In addition, the Budget announces the **Nature Recovery Network Fund**, which will partner with businesses and local communities to protect, restore and support existing habitats and wildlife. The government will also introduce the **Natural Environment Impact Fund** to help prepare green projects that could be suitable for commercial investment in order to encourage **private sector support for environmental restoration**.

**1.251** The UK's commitment to protecting the natural environment extends beyond Great Britain and Northern Ireland and into the UK Overseas Territories. The government is **tripling funding for the Darwin Plus programme to help protect and conserve the globally significant biodiversity found in UK Overseas Territories**.[73] This builds on the £220 million for biodiversity conservation in developing nations, and the doubling of UK international climate finance, announced by the Prime Minister at the UN General Assembly last year.

## Waste and recycling

**1.252** The government is committed to improving waste management, boosting recycling and reducing plastic pollution. Following consultation in spring 2019, **the government will introduce a new Plastic Packaging Tax from April 2022** to incentivise the use of recycled plastic in packaging and help tackle the scourge of plastic in the natural environment. An additional **£700,000 will establish the Extended Producer Responsibility scheme**, designed to encourage producers to make their packaging more recyclable and reduce the amount of unnecessary packaging in their products. (38)

**1.253** The government will also take action to fight waste crime. The Budget will provide funding for a **digital waste tracking system to provide better data on waste transport**, as well as £2 million to improve evidence on where **fly-tipping** happens and the best ways to deter it.

**1.254** Further details on carbon reduction measures in the Budget can be found in Chapter 2.

[71] '25 Year Environment Plan', Department for Environment, Food & Rural Affairs, January 2018.

[72] 'Provisional Woodland Statistics', Forestry Research, June 2019.

[73] 'Darwin Plus Projects Register', Darwin Initiative, March 2020.

# 2 Budget policy decisions

**2.1** Chapter 1 explains how the measures announced in the Budget support the Government's long-term strategy. This chapter sets out all Budget 2020 policy decisions. Unless stated otherwise, the decisions set out are ones which are announced at the Budget.

**2.2** Table 2.1 shows the cost or yield of all Budget 2020 decisions with a direct effect on PSNB in the years up to 2025-26. This includes tax measures, changes to Departmental Expenditure Limits (DEL) and measures affecting annually managed expenditure (AME).

**2.3** The government is also publishing the methodology underpinning the calculation of the fiscal impact of each policy decision. This is included in the supplementary document ''Budget 2020: policy costings' published alongside the Budget.

**2.4** The supplementary document 'Overview of Tax Legislation and Rates', published alongside the Budget, provides a more detailed explanation of tax measures.

**Table 2.1: Budget 2020 policy decisions (£ million)[1]**

| | Head[2] | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| **Investing in excellent public services** | | | | | | | |
| ***Spending review*** | | | | | | | |
| 1 Spending Round 2019 and set resource envelope for the Comprehensive Spending Review 2020 | Spend | -2,530 | -12,600 | -27,225 | -32,095 | -36,085 | -42,320 |
| 2 Delivering public service commitments including on health, schools, criminal justice system (resource spending)[3] | Spend | 0 | -1,430 | -2,685 | -2,795 | -2,825 | - |
| 3 EU contributions: benefit from contributions no longer paid and customs duties retained | Spend | 0 | +4,340 | +4,990 | +7,130 | +11,250 | +14,605 |
| 4 Farm Support: domestic direct payments[4] | Spend | 0 | -2,710 | - | - | - | - |
| ***Delivering excellent services*** | | | | | | | |
| 5 National Health Service: 40 hospitals, diagnostics, operational capital[5] | Spend | 0 | -1,065 | - | - | - | - |
| 6 Immigration Health Surcharge: increase to £624 with £470 rate for children and extend to EEA nationals | Tax | 0 | +150 | +355 | +355 | +360 | +355 |
| 7 Pensions: increase annual allowance taper threshold and adjusted income limit, reduce minimum annual allowance | Tax | 0 | -180 | -315 | -450 | -560 | -670 |
| 8 Prisons: maintenance[4,5] | Spend | 0 | -175 | - | - | - | - |
| 9 Policing: counter terrorism[4] | Spend | 0 | -80 | - | - | - | - |
| 10 Safer Streets Fund: CCTV and street lighting[4,6] | Spend | 0 | -15 | - | - | - | - |

| | Head[2] | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| 11 Public Works Loan Board: increase main rate, with reduced rates for social housing and infrastructure | Spend | +105 | +60 | +175 | +205 | +270 | +325 |
| **Supporting people and families** | | | | | | | |
| ***Tax*** | | | | | | | |
| 12 National Insurance: increase Primary Threshold and Lower Profit Limit to £9,500 in April 2020 | Tax | * | -2,110 | -2,185 | -2,360 | -2,370 | -2,370 |
| 13 Fuel duty: freeze for 2020-21 | Tax | 0 | -525 | -530 | -540 | -555 | -560 |
| 14 Alcohol Duty: freeze all rates for 2020-21[10] | Tax | -40 | -285 | -295 | -305 | -310 | -320 |
| 15 VAT: zero rate e-publications | Tax | 0 | -60 | -175 | -185 | -190 | -200 |
| 16 National Insurance: NICs holiday for employers of veterans in first year of civilian employment | Tax | 0 | 0 | -15 | -20 | -25 | -25 |
| 17 VAT: abolish VAT for female sanitary products from January 2021 | Tax | 0 | -5 | -15 | -15 | -15 | -15 |
| 18 Vehicle Excise Duty: change classification of new motorhomes from 12 March 2020 | Tax | * | -15 | -20 | -25 | -30 | -35 |
| ***Spending*** | | | | | | | |
| 19 Personal Independence Payments: reduce frequency of assessments | Spend | 0 | 0 | 0 | -55 | -75 | -90 |
| 20 Neonatal Leave: new entitlement to up to 12 weeks paid leave | Spend | 0 | 0 | 0 | 0 | -15 | -15 |
| 21 Housing Benefit: further shared accommodation rate exemptions | Spend | 0 | 0 | 0 | 0 | -10 | -15 |
| 22 Rough sleeping[4,5] | Spend | 0 | -60 | - | - | - | - |
| **Backing business** | | | | | | | |
| 23 Capital Allowances: increase structures and buildings allowance rate to 3% | Tax | -15 | -90 | -165 | -210 | -260 | -295 |
| 24 Research and Development Expenditure Credit: increase rate to 13% | Spend | 0 | * | -170 | -275 | -300 | -310 |
| 25 Employment Allowance: increase from £3,000 to £4,000 | Tax | 0 | -445 | -455 | -465 | -470 | -475 |
| 26 Business Rates: increase retail discount to 50%, and extend to cinemas and music venues for 2020-21 | Tax | +10 | -270 | -15 | 0 | 0 | 0 |
| 27 Business Rates: £1,000 discount for pubs with rateable value of less than £100,000 for 2020-21 | Tax | * | -20 | * | 0 | 0 | 0 |
| 28 Corporation Tax: relief for pre-2002 intangible fixed assets | Tax | -5 | -25 | -60 | -95 | -140 | -185 |
| 29 Enterprise: business productivity and locally delivered business support | Spend | 0 | -20 | - | - | - | - |
| **Levelling up and getting Britain building** | | | | | | | |
| 30 Spending Round 2019 and set capital envelope for the Comprehensive Spending Review 2020 | Spend | 0 | -2,450 | -13,690 | -14,465 | -13,610 | -22,500 |

| | Head[2] | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| 31 Delivering investment commitments including on transport, health, justice, education, R&D (capital spending)[7] | Spend | 0 | -3,290 | -4,315 | -6,160 | -8,150 | - |
| 32 Housing: building safety fund[4,5] | Spend | 0 | -1,215 | - | - | - | - |
| 33 Housing: brownfield housing fund[5] | Spend | 0 | -95 | - | - | - | - |
| 34 Culture: cultural investment fund, parklife, national museums maintenance[4,5] | Spend | 0 | -95 | - | - | - | - |
| **Growing a greener economy** | | | | | | | |
| 35 Ultra low emission vehicle grants[4,5] | Spend | 0 | -140 | - | - | - | - |
| 36 Air Quality[5] | Spend | 0 | -175 | - | - | - | - |
| 37 Renewable Heat Incentive: extend | Spend | 0 | 0 | -10 | -30 | -35 | -35 |
| 38 Plastic Packaging Tax: 30% recycled content threshold and £200 per tonne | Tax | 0 | 0 | 0 | +240 | +235 | +220 |
| 39 Red Diesel: remove relief for sectors other than rail, home heating and agriculture | Tax | 0 | 0 | +15 | +1,575 | +1,640 | +1,645 |
| 40 Climate Change Levy: two year extension to climate change agreement scheme and open to new entrants | Tax | 0 | * | -5 | -5 | -190 | -190 |
| 41 Climate Change Levy: increase gas rate in 2022-23 and 2023-24, freeze liquid petroleum gas and other commodities | Tax | 0 | 0 | 0 | +130 | +260 | +270 |
| 42 Capital Allowances for Business Cars: extend first year allowance on zero emission cars and raise eligibility criteria | Tax | 0 | * | -5 | +10 | +70 | +110 |
| 43 Carbon Price Support: freeze for 2021-22 | Tax | 0 | 0 | -20 | -15 | -15 | -15 |
| 44 Vehicle Excise Duty: exempt zero emission vehicles from the expensive car supplement | Tax | 0 | -10 | -15 | -20 | -30 | -45 |
| **A fair and sustainable tax system** | | | | | | | |
| 45 Corporation Tax: maintain at 19% | Tax | +930 | +4,635 | +6,120 | +6,680 | +7,075 | +7,500 |
| 46 Capital Gains Tax: reduce the lifetime limit in entrepreneurs' relief to £1,000,000 | Tax | +5 | +215 | +1,120 | +1,470 | +1,670 | +1,820 |
| 47 Stamp Duty Land Tax: 2% non-UK resident surcharge | Tax | 0 | +250 | -355 | +35 | +105 | +105 |
| 48 Tobacco Duty: extend RPI plus 2ppt escalator and additional 4ppt for hand rolling tobacco in 2020-21 | Tax | +5 | +30 | +35 | +30 | +15 | +5 |
| 49 Income Tax: top slicing relief amendments | Tax | 0 | * | -15 | -15 | -15 | -20 |
| 50 Digital Services Tax: technical changes | Tax | +65 | -5 | * | * | * | +70 |
| 51 Corporate Capital Loss Restriction: companies in liquidation | Tax | * | * | -5 | -5 | -5 | -5 |
| 52 Aggregates Levy: freeze for 2020-21 | Tax | 0 | -10 | -10 | -10 | -10 | -10 |
| 53 Heavy Goods Vehicle VED and Levy: freeze in 2020-21 | Tax | 0 | -10 | -10 | -10 | -10 | -10 |

| | Head[2] | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| 54 Car Fuel Benefit: increase by CPI in 2020-21 | Tax | 0 | +5 | +5 | +5 | +5 | +5 |
| 55 Savings: maintain £20,000 limit for adult ISA in 2020-21 | Tax | 0 | * | * | * | * | +5 |
| **Avoidance, evasion, and unfair outcomes** | | | | | | | |
| 56 Notification of uncertain tax treatment | Tax | * | +10 | +20 | +40 | +45 | +45 |
| 57 Tackling abuse in the construction industry scheme | Tax | 0 | 0 | 0 | +20 | +20 | +15 |
| 58 Conditionality: hidden economy | Tax | 0 | 0 | +5 | +35 | +50 | +65 |
| 59 Investment in HMRC to improve tax compliance | Tax | +55 | +280 | +855 | +1,065 | +1,075 | +595 |
| 60 Research and Development PAYE Cap: delay by one year and updated design | Spend | 0 | 0 | -60 | -130 | -65 | -35 |
| 61 Housing Benefit: investment in fraud detection by Local Authorities | Spend | 0 | +115 | +140 | +125 | +105 | +60 |
| **Financial transactions** | | | | | | | |
| 62 Public sector net borrowing impact of financial transaction changes[8] | Spend | +2,160 | +2,530 | +2,900 | +3,155 | +990 | +985 |
| **Previously announced policy decisions** | | | | | | | |
| 63 Independent Loan Charge Review: implementation of the recommendations | Tax | -30 | -305 | -245 | -70 | -70 | -25 |
| 64 Windrush: tax exemption for compensation payments | Tax | * | -5 | -5 | * | * | * |
| 65 Protecting Your Taxes in Insolvency: delay start date to December and extend to Northern Ireland | Tax | -5 | -30 | -85 | -35 | +5 | +5 |
| 66 Company Car Tax: temporary reduction for new cars registered from 6 April 2020 | Tax | 0 | -50 | -50 | * | 0 | 0 |
| 67 Stamp Tax on Shares: connected company transfers | Tax | 0 | +5 | +5 | +5 | +5 | +5 |
| 68 VAT: change start date for reverse charge for building and constructions services | Tax | -85 | -60 | +20 | +15 | 0 | 0 |
| 69 Business Rates Retention Pilots: 2020-21 pilots in Devolution Deal areas and the Greater London Authority | Spend | 0 | -150 | +45 | 0 | 0 | 0 |
| 70 Negative Revenue Support Grant: eliminate in 2020-21 | Spend | 0 | -65 | 0 | 0 | 0 | 0 |
| 71 Communities: youth investment fund[4,5] | Spend | 0 | -80 | - | - | - | - |
| 72 Welfare: restrict EEA migrants' access to non-contributory benefits for first five years in UK from January 2021 | Spend | 0 | * | +5 | +25 | +50 | +80 |
| 73 Child Benefit and Child Tax Credits: end exporting for children outside the UK from January 2021 | Spend | 0 | * | * | * | +5 | +5 |
| 74 Universal Credit: delay surplus earnings threshold reduction by one year | Spend | 0 | -75 | 0 | 0 | 0 | 0 |

| | Head[2] | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| 75 Universal Credit: additional support for claimants transferring to pension credit | Spend | 0 | -5 | -10 | -10 | -15 | -25 |
| 76 Universal Credit: changes to severe disability premium regulations | Spend | -10 | -5 | -5 | * | * | 0 |
| **Total policy decisions[9]** | | **+605** | **-17,900** | **-36,430** | **-38,530** | **-41,150** | **-41,920** |
| **Total spending policy decisions[9]** | | -355 | -19,255 | -40,185 | -45,640 | -48,780 | -49,440 |
| *Of which current* | | *-2,545* | *-13,765* | *-24,910* | *-27,860* | *-27,680* | *-27,660* |
| *Of which capital* | | *+2,190* | *-5,490* | *-15,275* | *-17,775* | *-21,100* | *-21,780* |
| **Total tax policy decisions[9]** | | +960 | +1,355 | +3,755 | +7,110 | +7,625 | +7,520 |

* Negligible.

[1] Costings reflect the OBR's latest economic and fiscal determinants.

[2] Many measures have both tax and spend impacts. Measures are identified as tax or spend on the basis of their largest impact.

[3] The overall spending level in 2024-25 has been adjusted for the costs of these measures. Settlements for 2024-25 will be set out at the Spending Review after the Comprehensive Spending Review 2020.

[4] The overall resource spending envelope has been adjusted to include funding for this measure in future years. Settlements over the period 2020-21 to 2023-24 will be set out in full at the Comprehensive Spending Review 2020.

[5] These costs are additional capital spending in 2020-21. Future profiles and total programme costs for some specific programmes are detailed elsewhere in the document. Settlements beyond 2020-21 will be set out in full at the Comprehensive Spending Review 2020.

[6] Safer Streets Fund: There is a total of £25m in this Fund, of which £10m is funded from the Home Office settlement.

[7] Departments have existing 2020-21 capital budgets. Some additions were made to 2020-21 capital budgets at the Spending Review 2019 and further additions are made at this Budget. Years beyond 2021-22 represent the overall capital envelope, which will be allocated to departments at the Comprehensive Spending Review 2020. Some specific capital allocations are set out throughout this document.

[8] Further details on financial transactions is set out in the financial transaction table.

[9] Totals may not sum due to rounding.

[10] The modelling for this measure was corrected after this table was finalised. The accompanying published costing note contains the updated impacts on the public finances.

# National Living Wage and welfare

**2.5 Publishing the Low Pay Commission's 2020 Remit** – Alongside the Budget, the government has published its remit to the Low Pay Commission (LPC) for 2020. Confirming the government's ambitious target, the remit asks the LPC to make recommendations with the view of reaching a National Living Wage (NLW) of two-thirds of median earnings by 2024, provided economic conditions allow. Following recommendations made by the LPC, the NLW will apply to workers aged 23 and over in April 2021, with a target for it to apply to workers aged 21 and over by 2024.

**2.6 Carers' leave** – The government will shortly consult on the design of Carers' Leave: a new in-work entitlement for employees with unpaid caring responsibilities, such as for a family member or dependents. This will support hardworking people to balance their caring responsibilities with work, particularly women who disproportionately undertake unpaid caring activities.

**2.7 Neonatal leave and pay** – The Budget announces a new entitlement to neonatal leave and pay for employees whose babies spend an extended period of time in neonatal care. (20)

**2.8 Personal Independence Payment reassessments** – The government will reduce the frequency of health assessments required for people receiving Personal Independence Payment (PIP). For those whose condition is unlikely to change, the Budget sets a minimum award review length of 18 months. (19)

**2.9 Increase in the repayment period for Universal Credit advances and reduction in the maximum debt deduction cap on the Universal Credit standard allowance** – From October 2021, the period over which Universal Credit advances will be recovered will increase to 24 months, while the maximum rate at which deductions can be made from a Universal Credit award will reduce from 30% to 25% of the standard allowance.

**2.10 Enhancing Housing Benefit compliance** – The Budget provides further investment of up to £12 million per year in local authority resource to maximise their capacity to tackle Housing Benefit fraud and error. (61)

**2.11 Universal Credit to Pension Credit transition** – The Budget confirms funding for an operational change to ensure claimants do not experience a gap in their benefit entitlement when moving from Universal Credit to Pension Credit. (75)

**2.12 Universal Credit: transitional protection for former Severe Disability Premium (SDP) claimants** – The government is confirming funding for increasing the rate of transitional payments for claimants in receipt of Severe Disability Premium when they move to Universal Credit. (76)

**2.13 Universal Credit rollout** – The implementation schedule of Universal Credit has been updated to ensure its safe delivery. The government expects rollout to complete by September 2024.

**2.14 Universal Credit: surplus earnings** – The Budget confirms funding for a delay to the reduction of the Universal Credit surplus earnings threshold, so that only large income spikes above £2,500 will be taken into account. The threshold will be reduced to £300 in April 2021. (74)

**2.15 Changes to the duration of high level sanctions** – The government is removing the three-year sanction from Universal Credit and Jobseeker's Allowance. This will bring high-level sanctions to 13 weeks for the first failure to comply with conditionality or work search requirements and 26 weeks for each subsequent failure, making 26 weeks the duration of the longest single sanction in Universal Credit and Job Seekers Allowance.

**2.16 Supporting families with school-aged children through Tax-Free Childcare (TFC)** – The government is announcing a service improvement that will make TFC compatible with school payment agents. This will allow parents of up to 500,000 school-aged children across the UK to access TFC and use it towards the cost of their wraparound childcare.

**2.17 Migrants' access to benefits** – The government is aligning EEA migrants' access to non-contributory benefits with non-EEA nationals. This will apply to EEA migrants arriving in the UK under the new immigration system, from January 2021. (72)

**2.18 Stop export of Child Benefit** – The government is stopping the export of Child Benefit payments made in respect of children living overseas. This will apply to EEA migrants arriving in the UK under the new immigration system, from January 2021. (73)

**2.19 Porting of Support for Mortgage Interest (SMI) loans** – As announced in June 2019, the government will amend the SMI loan regulations to allow recipients moving home to transfer their existing loan to their new property.

**2.20 Extending Shared Accommodation Rate (SAR) exemptions** – The government is introducing exemptions from the SAR for claimants of Universal Credit and Housing Benefit covering rough sleepers aged 16-24, care leavers up to the age of 25, and victims of domestic abuse and human trafficking. (21)

**2.21 Extension to Civil Partnerships: State Pension** – The Civil Partnerships (Opposite-sex Couples) Regulations 2019 give opposite-sex couples the choice of entering into marriage or civil partnership. The Budget provides funding which ensures individuals can derive or inherit a State Pension from an opposite-sex civil partner.

**2.22 Devolution of welfare benefits to the Scottish Government** – As set out in the Scotland Act 2016, the government is devolving a number of disability benefits to the Scottish government, including Personal Independence Payment, Disability Living Allowance, Attendance Allowance, Industrial Injuries Disablement Allowance and Severe Disablement Allowance.

# Public spending decisions

## Health

**2.23 Nurses** – From September 2020, all new and existing students on nursing, midwifery and allied health courses in England will benefit from additional non-repayable maintenance grants to help with living costs. Students will receive at least £5,000 a year, with up to £3,000 further financial support available for eligible students with childcare responsibilities, as well as those studying in regions and specialisms where Trusts find it difficult to recruit nurses.

**2.24 50 million GP surgery appointments** – The government is committed to creating 50 million more GP surgery appointments a year in England. The government will achieve this by funding the Department for Health and Social Care and the NHS to train, recruit and retain up to 6,000 more doctors in general practice and 6,000 more primary care professionals, such as physiotherapists and pharmacists.

**2.25 Health Infrastructure Plan (HIP)** – As announced in September 2019, the government has committed £2.7 billion to deliver 6 major building and redevelopment schemes in hospitals in England, and a further £100 million of seed funding for other schemes to develop their plans. In total, this programme involves at least 40 hospital building projects. (5)

**2.26 Learning Disability and Autism Fund** – The government will provide funding over the next three years to speed up the discharge of individuals with learning disabilities or autism into the community from mental health inpatient care in England.

**2.27 NHS operational capital** – The government will protect the level of NHS operational capital investment in England by increasing the DHSC's capital budget by £683 million in the new financial year 2020-21. This will allow Trusts to continue to invest in important capital projects such as estate refurbishments and building maintenance. (5)

**2.28 National Institute for Health Research (NIHR)** – In order to improve our understanding of how to reduce the burden of illness in the future, the government is committing £12 million of new funding for the National Institute for Health Research to invest in prevention research, supporting local authorities to grow their research capabilities for the longer term.

**2.29 Diagnostic equipment replacement** – As announced in September 2019, the government is providing £200 million for the NHS in England to replace its oldest diagnostic equipment, including MRI machines, CT scanners, and breast screening equipment. The new equipment will improve the quality of screening and speed of diagnosis for illnesses such as cancer. (5)

**2.30 Hospital car parking** – The government will scrap hospital car parking fees in England for those in greatest need, including patients with a disability and/or terminal illness and their families, patients with regular appointments, parents of sick children staying overnight and NHS staff working night shifts.

**2.31 Immigration Health Surcharge (IHS)** – The government will increase the IHS from £400 to £624. There will be a new discounted rate for children under the age of 18 of £470. For students and those entering on the youth mobility scheme, the surcharge will rise from £300 to £470. (6)

## Safety and security

**2.32 Counter terrorism** – Overall counter-terrorism spending will increase by £114 million in 2020-21 to maintain capability and officer numbers in the face of a changing terrorist threat, and to help keep the UK safe. This includes an additional £31 million for the UK Intelligence Community and £83 million for counter-terrorism policing. As a result, funding for counter-terrorism policing will increase by £103 million in 2020-21. (9)

**2.33 UK Intelligence Community infrastructure** – The government has provided the UK Intelligence Community with £67 million additional funding to build on their world-leading technological capabilities so that they can continue to help keep the country safe from harm.

**2.34 Capital for Companies House** – The government will allocate £14 million to Companies House to enable it to continue with vital capital projects to help its work tackling economic crime and anti-money laundering.

**2.35 Fire Safety** – The government is providing £20 million for Fire and Rescue Services to increase inspection and enforcement capability and build a strategic response to the Grenfell Public Inquiry's findings.

**2.36 Domestic violence prevention** – The government is providing £10 million in 2020-21 for innovative new approaches to preventing domestic abuse, working with Police and Crime Commissioners to expand projects like the "Drive" prevention programme.

**2.37 Domestic abuse courts** – The government will provide an additional £5 million to begin a trial of integrated domestic abuse courts in England and Wales. This funding will allow progress to be made on establishing these courts over the next year.

**2.38 Royal Commission on the Criminal Justice process** – The government will provide an additional £3 million to launch a Royal Commission on the Criminal Justice process in England and Wales. This funding will allow work on the Commission to begin at pace over the next year.

**2.39 Community sentences** – The government will provide an additional £68.5 million to strengthen community sentences in England and Wales, including by increasing the number of offenders who are required to wear an electronic tag.

**2.40 Victim support** – The government will provide an additional £15 million to improve the justice system's offer to victims. This will boost the support available to victims of rape, and create a new digital hub to make the criminal justice process in England and Wales easier to understand.

**2.41 Prison maintenance** – The government will provide an additional £156 million in 2020-21 to tackle prison maintenance issues, helping to maintain prison operating capacity and improve conditions for those living and working in prisons in England and Wales. (8)

**2.42 Youth Violence** – The government is providing £5 million in 2020-21 to support the creation of a Centre of Excellence for Tackling Youth Violence.

**2.43 Economic crime levy** – The government intends to introduce a levy to be paid by firms subject to the Money Laundering Regulations to help fund new government action to tackle money laundering and ensure delivery of the reforms committed to in the Economic Crime Plan.[1] These reforms will help safeguard the UK's global reputation as a safe and transparent place to conduct business. The levy will be additional to ongoing public sector funding. The government will publish a consultation on the levy later this spring.

### Armed forces

**2.44 Additional funding for veterans mental health** – The government will provide a £10 million uplift in 2020-21 to the Armed Forces Covenant Fund Trust, to deliver charitable projects and initiatives that support veterans with mental health needs. This funding demonstrates this government's ongoing commitment to ensuring that our veterans can access the services and support that they deserve.

**2.45 Southampton Spitfire Memorial** – The government will provide up to £3 million match-funding to support the construction of a memorial to the Spitfire on the Southampton waterfront, in recognition of the individuals who built and flew the aircraft in the Second World War.

## Education and skills

**2.46 Further education capital funding** – The government will provide £1.5 billion over five years (£1.8 billion inclusive of indicative Barnett consequentials), supported by funding from further education colleges themselves, to bring the facilities of colleges everywhere in England up to a good level, and to support improvements to colleges to raise the quality and efficiency of vocational education provision.

[1] 'Economic crime plan 2019 to 2022', HM Treasury and Home Office, July 2019.

**2.47 Institutes of Technology** – The government will provide £120 million to bring further education and higher education providers in England together with employers to open up to eight new Institutes of Technology. These institutions will be used to deliver high-quality higher level technical education and to help close skills gaps in their local areas.

**2.48 Facilities and equipment to support T levels** – The government will provide £95 million for providers in England to invest in high quality facilities and industry-standard equipment to support the rollout of T levels. Funding will support T level routes being delivered from autumn 2021, including construction, digital, and health and science.

**2.49 National Skills Fund** – The government will consult widely in the spring on how to use the new National Skills Fund.

**2.50 Apprenticeship Levy** – The government will look at how to improve the working of the Apprenticeship Levy, to support large and small employers in meeting the long-term skills needs of the economy.

**2.51 Apprenticeships** – The government will ensure that sufficient funding is made available in 2020-21 to support an increase in the number of new high-quality apprenticeships in small- and medium-sized businesses.

**2.52 Maths schools** – The government will provide an additional £7 million to support a total of 11 maths schools in England, covering every region.

**2.53 PE and sports** – The Budget provides £29 million a year by 2023-24 in England to support primary school PE teaching and help schools make the best use of their sports facilities.

**2.54 Arts Premium** – The Budget provides £90 million a year to introduce an Arts Premium from September 2021, to help schools in England to provide high-quality arts programmes and extracurricular activities for pupils.

**2.55 Freezing the maximum fee cap** – As announced in July 2019, the government has frozen the maximum fee cap in England for the 2020-21 academic year at £9,250 for regular full-time undergraduate courses and at £11,100 for accelerated degree courses.

**2.56 Removing the student finance three-year residence requirement for victims of domestic abuse** – From academic year 2020-21, the government is removing the three-year ordinary residence requirement for student finance for those granted Indefinite Leave to Remain as victims of domestic abuse.

**2.57 Entitlement to part-time Maintenance Loans** – The Budget takes into account the fiscal impacts of part-time Maintenance Loans not being extended to sub-degree (level 4/5 courses) and distance learners, as announced in June 2019 and March 2019 respectively.

## Local government and communities

**2.58 Local Infrastructure Rate lending** – The government will provide an additional £1.15 billion discounted lending at 60 basis points above gilts via the Public Works Loan Board (PWLB) to support specific local authority infrastructure projects for England, Scotland and Wales. (11)

**2.59 Housing Revenue Account lending rate** – The rate for discounted PWLB lending to support social housing will be reduced to 80 basis points above gilts for local authorities in England, Scotland and Wales. (11)

**2.60 Future of Public Works Loan Board lending terms** – The government will consult on revising the terms of PWLB lending to ensure that local authorities can continue to invest in housing, infrastructure and frontline services.

**2.61 Public Works Loan Board powers** – The government will reset its power to increase the PWLB lending limit.

**2.62 Adults with multiple complex needs** – The government will commit £46 million from the Shared Outcomes Fund to provide improved support to individuals experiencing multiple complex needs, such as homelessness, reoffending and substance misuse.

**2.63 Rough sleeping** – The Budget confirms the £237 million announced by the Prime Minister for accommodation for up to 6,000 rough sleepers and provides a further £144 million for associated support services and £262 million for substance misuse treatment services which, when fully deployed, is expected to help more than 11,000 people a year. This will enable people to move off the streets and support them to maintain a tenancy for the long term. (22)

**2.64 Research to support vulnerable children** – This Budget will go further on supporting families by providing £2.5 million for research and developing best practice around the integration of services for families, including family hubs, and how best to support vulnerable children.

**2.65 Increased Business Rates Retention in Devolution Deal areas and the Greater London Authority** – In 2017-18, the government set-up 100% Business Rates Retention pilots in devolution deal areas: Cornwall, Greater Manchester, Liverpool City Region, West of England and West Midlands. London has also benefitted from increased retention arrangements from 2017-18. These areas will continue to benefit from increased retention, and London will receive 67% retention in 2020-21, in line with the Greater London Authority funding agreement made in 2017-18. (69)

**2.66 Eliminating negative Revenue Support Grant (RSG) in 2020-21 –** The government confirmed at the 2020-21 Local Government Finance Settlement that it will eliminate negative RSG through the use of foregone business rates, at a cost of £153 million. This is to maintain the commitment not to adjust business rates tariffs and top-ups until the business rates retention system is reset. (70)

## Public sector capability

**2.67 Data sharing** – The government has already improved its use of data through the Artificial Intelligence and Data Grand Challenge and the ONS Data Science Campus. The Budget goes further by investing £16.4 million over the next three years, including £6.8 million for the ONS to make it easier to share more, higher-quality data across government. This will improve policy making and evaluation, and combine datasets in new ways to detect fraud. This investment is a first step in the government's National Data Strategy to unlock the power of data across government and the wider economy, while building trust in its use.

**2.68 General grants transformation program** – General grants are awarded to an organisation for an agreed purpose and are considered the category of grants with the highest risk of being spent ineffectively. The government is launching a new £5 million programme to create digital tools to increase efficiencies and improve administration of general grants.

**2.69 Public Sector Value Framework** – The government is developing the medium- to long-term priority outcomes that it is seeking to deliver for priorities such as levelling up, as well as the metrics that will be used to inform and improve performance against these outcomes. These will be published as part of the CSR and will include cross-cutting outcomes in areas where closer working between departments could help achieve better results.

**2.70 Building commercial capability** – Central government spends £50 billion per year on third-party goods and services. The contracts governing these arrangements are often complex and require considerable expertise to manage effectively. The government will therefore provide £3 million of funding for face-to-face training and assessment of staff across government who manage the most important contracts. By further upskilling key staff, government can improve the efficiency and performance of its largest contracts.

## Culture

**2.71 Cultural Investment Fund** – The government confirms a £250 million Cultural Investment Fund for culture, heritage, local museums, and neighbourhood libraries. Of this, £90 million will be made available from April for a Cultural Development Fund that will support cultural regeneration proposals outside of London. (34)

**2.72 Youth Investment Fund** – The Budget confirms £500 million for a Youth Investment Fund to build new youth centres, refurbish existing youth facilities and provide high-quality services for young people across the country. The government expects that at least 800,000 young people will benefit from new or upgraded youth facilities.

**2.73 National Museums maintenance** – The government is providing £27 million for critical maintenance work on the National Museums' estates. The government understands the maintenance challenges faced by the National Museums and will take further action to address these at the CSR.

**2.74 Football Foundation scheme** – The Budget commits £8 million investment in local football facilities alongside matched funding from the Premier League and Football Association, providing quality football facilities in areas with the greatest need. (34)

## Infrastructure

**2.75** The government will publish a landmark National Infrastructure Strategy later in the spring which will set out plans for a once in a generation transformation of the UK's economic infrastructure. This will respond to the recommendations of the National Infrastructure Commission's (NIC) National Infrastructure Assessment.[2]

**2.76 Economic regulation** – The government is committed to maintaining the UK's system of strong, independent regulation. The government therefore welcomes the NIC's report 'Strategic investment and public confidence' and agrees with its primary finding that the UK's system of economic regulation is working well, but may need updating in some areas to address 21st century challenges.[3] The government will respond in full to the study later this year.

**2.77 Reviewing PFI contracts** – The government has retired the PFI and PF2 models, but there are nearly 600 existing PFI contracts in England.[4] The government will now focus on making sure they are well managed and represent value for money and will allocate £2 million in 2020-21 to carry out targeted contract reviews.

### Digital connectivity

**2.78 Gigabit broadband** – The Budget commits £5 billion to support the rollout of gigabit-capable broadband in the most difficult to reach 20% of the country.

[2] 'National Infrastructure Assessment', National Infrastructure Commission, July 2018.

[3] 'Strategic investment and public confidence', National Infrastructure Commission, October 2019.

[4] 'Private Finance Initiative and Private Finance 2 projects: 2018 summary data', HM Treasury and Infrastructure and Projects Authority, May 2019.

**2.79 New build homes' connectivity** – The Budget announces that DCMS will shortly publish a consultation response which will confirm the government's intention to legislate to ensure that new build homes are built with gigabit-capable broadband.

**2.80 Existing broadband programmes** – As part of over £1 billion that the government has already committed to next-generation digital infrastructure, the Budget announces:

- the next seven areas that have successfully bid for funding from the third wave of the Local Full Fibre Networks Challenge Fund: North of Tyne (£12 million), South Wales (£12 million), Tay Cities (£6.7 million), Pembrokeshire (£4 million), Plymouth (£3 million), Essex and Hertfordshire (£2.1 million) and East Riding of Yorkshire (£1 million)
- that the government's existing superfast broadband programme has shifted its focus to delivering gigabit-capable broadband and has already delivered full fibre to over 370,000 premises
- that more than 100 schools in rural areas are due to receive full fibre broadband in the next twelve months under the Rural Gigabit Connectivity programme

**2.81 Shared Rural Network to improve 4G coverage** – The Budget announces that the Shared Rural Network agreement has been finalised between the government and industry. The government will commit up to £510 million of funding, which will be more than matched by industry to support this scheme to improve mobile coverage. This means 95% of the UK's landmass will have high quality mobile coverage by 2025.

## Transport

**2.82 Second Road Investment Strategy (RIS2)** – The government is boosting regional connectivity and transforming connections through the largest ever investment in England's strategic roads.[5] Through RIS2 the government will spend over £27 billion between 2020 and 2025. It will take forward schemes such as:

- dualling the A66 Trans-Pennine and upgrading the A46 Newark bypass, addressing congestion on these key routes in the North East and the Midlands
- improving the M60 Simister Island in Manchester to tackle delays
- building the Lower Thames Crossing, which will increase road capacity across the Thames east of London by 90%[6]
- building a new, high-quality dual carriageway and a two-mile tunnel in the South West to speed up journeys on the A303, and to remove traffic from the iconic setting of Stonehenge
- considering how the A1/A19 north of Newcastle and the A1 Doncaster to Darrington in Yorkshire can be improved to speed up journeys and boost economic growth
- exploring how to connect communities in East Lancashire and West Yorkshire better, and exploring the case for improvements to links between the M4 and the Dorset Coast

**2.83 Midlands Rail Hub** – The government is investing £20 million to develop the Midlands Rail Hub, progressing plans for a major programme of improvements to rail services between the regions' cities.

**2.84 Transforming Cities Fund** – The Budget allocates over £1 billion from the Transforming Cities Fund. This will deliver a range of schemes by 2022-23, including:

---

[5] 'Departmental update', Department for Transport, October 2019.

[6] 'Lower Thames Crossing', Highways England.

- £79 million for Bournemouth, Christchurch & Poole, including four new cycle freeways and new bus priority infrastructure
- £161 million for Derby & Nottingham, including over £25 million for bus rapid transit in Derby and over £10 million for a new cycle route between Nottingham, Derby and East Midlands Airport
- £33 million for Leicester, including £8 million for the development of a sustainable transport corridor from St Margaret's to Birstall
- £198 million for the North East, including £95 million for frequency and reliability improvements across the Tyne and Wear Metro system and to complement the government's recent £337 million investment in new rolling stock
- £51 million for Plymouth, including £36 million for an iconic new Central Park cycling and walking bridge
- £40 million for Preston City Region, including £25 million for a new station at Cottam Parkway on the Preston-Blackpool line
- £166 million for Sheffield City Region, including a new Bus Rapid Transit link in Barnsley and a new tram stop on the Tram-Train line to Rotherham at Magna
- £57 million for Southampton, including new Rapid Bus links
- £317 million for West Yorkshire, including £39.9 million for Halifax delivering a new bus station, improved rail station and other improvements to complement the revitalisation of the town centre and £30 million for active and sustainable travel across Bradford
- a further £117 million for Portsmouth City Region, Norwich and Stoke-on-Trent subject to further business case approval, which could fund a range of projects, including a multi-modal transport hub at Stoke-on-Trent station

**2.85 Intra-city transport settlements** – The government is investing £4.2 billion in the transport networks of eight city regions across England from 2022-23. Funding will be delivered through five-year, consolidated transport settlements agreed with central government and based on plans put forward by Mayors. Following the approach that has worked for London, these settlements will be published once they have been agreed, providing transparency and accountability while giving Mayors the flexibility and certainty to deliver their plans. As a first step, the government will open discussions with Greater Manchester, Liverpool City Region and West Midlands in the coming months. The new West Yorkshire Combined Authority, Sheffield City Region, Tyne and Wear, West of England and Tees Valley will also receive settlements, subject to putting in place appropriate governance to agree and deliver funding, including an elected Mayor for their city regions and transport networks. Resource funding to support the city regions with planning and delivery of these settlements will be set out at the CSR.

**2.86 Local road upgrades** – The Budget announces the second round of successful Major Road Network and Large Local Major schemes proceeding to the next stage of development. This includes the:

- junction improvements to the A12 East of Ipswich
- improving the A350 at Junction 17 of the M4
- a single carriageway bypass on the A39 Atlantic Highway
- junction improvements to the A426/A4071 Avon Mill/Hunters Lane, and a short dual carriageway

- a link road from Chesterfield town centre to the A6192 and A619 at Staveley
- carriageway dualling and roundabout improvements on the A12 in Woodbridge
- junction improvements on the A127 growth corridor
- capacity enhancement on the A326
- alleviating congestion pinch points through the villages of Walton and Ashcott on the A39
- junction improvements at the Army and Navy roundabout near the centre of Chelmsford
- refurbishment of the flyover structure carrying the A232 in Croydon
- improving the Ely to Cambridge A10 Junction
- refurbishment to the Hope and Anchor flyover which carries the A316 Twickenham Road
- refurbishment of Kew Bridge
- upgrades to M5 Junction 9 and a bypass on the A46 Ashchurch

**2.87 Potholes fund** – The government is announcing £500 million per year from 2020-21 to 2024-25 to help tackle potholes and to stop them from forming. As a result, the government will spend £1.5 billion in 2020-21 on filling in potholes and resurfacing roads.

**2.88 Station accessibility funding** – The government will invest £50 million to improve accessibility at 12 stations, including Newtown in Powys, Beeston in Nottinghamshire, Eaglescliffe in County Durham, and Walkden in Greater Manchester. This will expand the programme of station upgrades being undertaken through the Department for Transport's Access for All initiative.

**2.89 Changing Places Fund** – The government is determined to see greater provision of Changing Places toilet facilities in new and existing buildings. These facilities are designed to provide sufficient space and equipment for people who are not able to use the toilet independently. Following on from a consultation in 2019, the government will change building regulations guidance by the end of this year to mandate the provision of Changing Places toilets in new public buildings. The Budget also confirms that the government will launch a £30 million Changing Places Fund, working with the Changing Places Consortium and others to identify those sectors where we most need to accelerate the provision of such facilities in existing buildings.

**2.90 Local transport supply chain study** – The CSR will set out further plans for investment in local transport spending. To inform these plans, the Infrastructure and Projects Authority will, working with departments, lead a study into supply chain capacity in order to assess how industry can best deliver the government's ambitious plans.

## Housing investment

**2.91 Affordable Homes Programme** – The Budget announces an additional £9.5 billion for the Affordable Homes Programme. In total, the programme will allocate £12.2 billion of grant funding from 2021-22 to build affordable homes across England. This should bring in a further £38 billion in public and private investment. This new five-year programme will help more people into homeownership and help those most at risk of homelessness.

**2.92 Housing infrastructure allocations** – The Budget confirms allocations from the Housing Infrastructure Fund totalling £1.1 billion for nine different areas, including Manchester, South Sunderland and South Lancaster. These successful bids will unlock up to 69,620 homes

and will help to stimulate housing and infrastructure growth across the country. The Budget also announces additional housing investments in York Central, Harlow and North Warwickshire totalling £328 million.

**2.93 Single Housing Infrastructure Fund** – At the CSR, the government will launch a new long-term Single Housing Infrastructure Fund to unlock new homes in areas of high demand across the country by funding the provision of strategic infrastructure and assembling land for development.

**2.94 Brownfield Housing Fund** – To level up all regions of the country, the Budget launches a new £400 million brownfield fund for pro-development councils and ambitious Mayoral Combined Authorities with the aim of creating more homes by bringing more brownfield land into development. The government will shortly invite bids that are ambitious and represent a significant increase in housing supply on brownfield land. The government will consider proposals from areas such as the West Midlands Combined Authority to expand their existing brownfield land fund. (33)

**2.95 Future Homes Standard** – The government is committed to reducing emissions from homes and to helping keep household energy costs low now and in the future. In due course, the government will announce plans to improve the standards of new built homes.

**2.96 Building Safety Fund** – Following the Grenfell tragedy, one of the government's most important objectives is to ensure residents feel safe and secure in their home. Having taken expert advice, the Budget confirms an additional £1 billion to remove unsafe cladding from residential buildings above 18 meters to ensure people feel safe in their homes. (32)

**2.97 HM Land Registry (HMLR)** – HMLR will be provided with £392 million to transition from a Trading Fund into part of central government. This funding includes £350 million that will be offset by HMLR returning its income to the Exchequer, and £42 million of funding to allow HMLR to continue with its ongoing project to digitise land registration in England and Wales, and enable further innovation in the property market and the wider UK economy.

## Floods and water

**2.98 Flood defences** – Starting in 2021, the government will invest £5.2 billion in a six-year capital investment programme for flood defences. This investment will better protect 336,000 properties from flooding.

**2.99 Place-based resilience schemes** – The government is confirming a new £200 million package of place-based resilience schemes to ensure faster recovery for rural, urban and coastal communities most at risk of flooding.

**2.100 Winter flood defence fund** – The government will provide £120 million to repair flood defences which were damaged in the floods in winter 2019-20.

**2.101 Water management assets** – The government will invest £39 million in the Environment Agency's network of water supply and water navigation assets. This investment will help provide upfront funding for asset repairs, which will ensure that waterways remain open and navigable, while contributing to flood and drought mitigation.

## Decarbonising power, industry and heat

**2.102 Energy Innovation Programme** – The government will at least double the size of the Energy Innovation Programme, with exact budgets to be decided at the CSR.

**2.103 Carbon Capture and Storage (CCS)** – The government will establish CCS in at least two UK sites, one by the mid-2020s, a second by 2030. This will be supported by the creation of a new CCS Infrastructure Fund of at least £800 million, with budgets to be finalised at the CSR.

**2.104 Support for at least one CCS power station by 2030** – Using consumer subsidies, the government will support the construction of the UK's first privately financed gas CCS power station.

**2.105 Green Gas Levy** – The government will consult on introducing levy-funded support for biomethane production to increase the proportion of green gas in the grid.

**2.106 Low carbon heat support** – The government will consult on introducing a new grant scheme from April 2022 to help households and small businesses invest in heat pumps and biomass boilers, backed by £100 million of new Exchequer funding.

**2.107 The Renewable Heat Incentive (RHI)** – The government will extend the Domestic RHI in Great Britain until 31 March 2022. It will also introduce a new allocation of flexible tariff guarantees to the Non-Domestic RHI in Great Britain in March 2021, helping to provide investment certainty for the larger and more cost-effective renewable heat projects. (37)

**2.108 Heat Networks** – The Budget confirms £96 million for the final year of the Heat Networks Investment Project, which ends in March 2022. After this, the government will invest a further £270 million in a new Green Heat Networks Scheme, enabling new and existing heat networks to be low carbon and connect to waste heat that would otherwise be released into the atmosphere.

**2.109 Net zero policy development** – The government is allocating an additional £10 million in 2020-21 to support the design and delivery of net zero policies and programmes.

## Reducing vehicle pollution

**2.110 Electric vehicle charging infrastructure investment and review** – The government will provide £500 million over the next five years for electric vehicle charging infrastructure. This will include a Rapid Charging Fund to help businesses with the costs of connecting high-powered charge points to the electricity grid, where those costs would prevent private sector investment. To target spending from this fund effectively, the Office for Low Emission Vehicles will complete a comprehensive review of electric vehicle charging infrastructure. This will build on the previous review announced in July 2019, extending its scope to cover the full Strategic Road Network and other strategic locations in cities and rural areas.

**2.111 Consumer incentives for the purchase of ultra-low emission vehicles** – The government is considering the long-term future of consumer incentives to support the transition to zero emission vehicles alongside the consultation on bringing forward the phase-out date for the sale of new petrol and diesel cars and vans from 2040. In the meantime, the government will provide £403 million for the Plug-in Car Grant, extending it to 2022-23. The government will also provide £129.5 million to extend the Plug-in Van Grant, Plug-in Taxi Grant, and Plug-in Motorcycle Grant to 2022-3. (35)

**2.112 Air quality** – The government will provide an additional £304 million to reduce nitrogen dioxide emissions. This brings the total funding provided for local authorities to deliver their air quality plans to £880 million. (36)

## Natural environment

**2.113 Nature for Climate Fund** – The government will invest £640 million in afforestation and peatland restoration in England, delivering more than a 600% increase in current tree planting rates.[7]

**2.114 Nature Recovery Network Fund** – The government will invest up to £25 million in England to partner with landowners, businesses, and local communities in the creation of Nature Recovery Areas. These will deliver habitat and species restoration and recovery, alongside wider natural capital benefits.

**2.115 Natural Environment Impact Fund** – The government will commit up to £10 million to stimulate private investment and market-based mechanisms to improve and safeguard our environment.

**2.116 Darwin Plus expansion** – The government will triple the Darwin Plus programme to £10 million per year to support the conservation of the UK Overseas Territories' unique and globally significant biodiversity and help protect and enhance their natural environments.[8]

## Waste and recycling

**2.117 Extended Producer Responsibility** – The government will commit £700,000 to develop IT capability to administer the future Extended Producer Responsibility scheme for packaging.

**2.118 Digital waste tracking** – The government will invest £7.2 million in a national system to enable the smart tracking of waste movements across the economy.

**2.119 Tackling fly-tipping** – The government will launch a £2 million fund to support innovative approaches to tackling fly-tipping.

## Growth across the country

**2.120 English Devolution White Paper** – The government will publish an English Devolution White Paper in the summer, setting out how it intends to meet its ambitions for full devolution across England.

**2.121 Local Growth Fund** – Decisions on the future of the Local Growth Fund will be made at the CSR. In advance of this, the Budget confirms up to £387 million in 2021-22 to provide certainty for local areas that they will be able to continue with existing priority Local Growth Fund projects that require funding beyond this year.

**2.122 West Midlands local growth funding** – The government is devolving over £160 million from the Local Growth Fund to West Midlands Combined Authority to accelerate progress on the Eastside Metro extension and phase one of the Sprint bus rapid transit network.

**2.123 West Yorkshire devolution deal** – The government has agreed a devolution deal with West Yorkshire to establish a Mayoral Combined Authority with a directly-elected Mayor from May 2021. This deal will provide £1.1 billion of investment for the area over 30 years, as well as devolving significant new powers to the area on transport, planning and skills. The deal also underpins the agreement of a long-term intra-city transport settlement for the region starting in 2022-23. Alongside this the government is providing up to £500,000 to support Bradford to develop plans that would maximise the benefits of potential Northern Powerhouse Rail connections.

---

[7] 'Provisional Woodland Statistics', Forestry Research, June 2019.

[8] 'Darwin Plus Projects Register', Darwin Initiative, March 2020.

**2.124 British Library at Leeds and Boston Spa** – The Budget makes available up to £95 million for the British Library site at Boston Spa. This investment will underpin the Library's plans to open a major new site in the centre of Leeds, creating a new British Library of the North. The government will provide a £25 million Heritage Fund to the West Yorkshire Combined Authority to support the Library in establishing this new site.

**2.125 UK Shared Prosperity Fund (UKSPF)** – The UKSPF will replace the overly-bureaucratic EU structural funds, levelling up opportunity in each of the four nations of the country. Funding will be realigned to match domestic priorities, with a focus on investing in people. It will, at a minimum, match current levels of funding to each nation from EU structural funds. The government will set out further plans for the Fund including at the CSR.

**2.126 Commonwealth Games trade and investment programme** – The Budget allocates £21.3 million for the Birmingham 2022 Commonwealth Games Trade, Tourism, and Investment Programme to take full advantage of the economic legacy for the West Midlands and the country as a whole from this exciting sporting event.

**2.127 Changing where the government makes decisions** – The government will relocate a minimum of 22,000 civil service roles out of central London, the vast majority to the other regions and nations of the UK. This will take place over the next decade via the Cabinet Office and its Places for Growth programme. HM Treasury, alongside DIT, BEIS and MHCLG, will establish a new economic decision-making policy campus of over 750 roles in the north of England. HM Treasury will also establish representation in Northern Ireland and Wales, adding to its existing presence in Scotland.

### The OxCam Arc

**2.128** The government has designated the corridor of land connecting Oxford, Milton Keynes, Bedford and Cambridge (the OxCam Arc) as a key economic priority. Earlier this year, the government announced the East West Rail Company's preferred route for the new line between Bedford and Cambridge. The government will also, subject to planning consents, build a new rail station at Cambridge South, improving connectivity to the world-leading research facilities of the Cambridge Biomedical Campus – the largest cluster of medical and life sciences research in Europe.

**2.129** The Budget announces plans to develop, with local partners, a long-term Spatial Framework to support strategic planning in the OxCam Arc. This will support the area's future economic success and the delivery of the new homes required by this growth up to 2050 and beyond. The government is also going to examine and develop the case for up to four new Development Corporations in the OxCam Arc at Bedford, St Neots/Sandy, Cambourne and Cambridge, which includes plans to explore the case for a New Town at Cambridge, to accelerate new housing and infrastructure development.

## Scotland, Wales, and Northern Ireland

**2.130 Scotland, Wales and Northern Ireland will receive significant funding through Barnett consequentials** for the devolved administrations to deliver public services, infrastructure and other priorities:

- the Scottish Government's block grant will increase by over £640 million through to 2020-21 before adjustments for tax devolution
- the Welsh Government's block grant will increase by over £360 million through to 2020-21 before adjustments for tax devolution – this includes a 5% uplift in Barnett consequentials agreed as part of the Welsh Government's fiscal framework in 2016

- the Northern Ireland Executive's budget will increase by over £210 million through to 2020-21

**2.131 Ofgem's estates programme** – The government will provide up to £2 million for Ofgem to secure new premises in Glasgow, increasing the number of staff operating outside of London.

**2.132 Funding allocations for remaining City and Growth Deals** – The government will provide funding for four City and Growth Deals in Scotland, Wales and Northern Ireland:

- £25 million for Argyll and Bute
- £55 million for Mid Wales
- £126 million for Mid, South and West of Northern Ireland, and £36 million for Causeway Coast and Glens

**2.133 Support for the whisky industry** – The government is expanding its support for the whisky industry by:

- freezing spirits duty for this year
- allocating £10 million for R&D spending to help decarbonise UK distilleries, including the whisky sector

**2.134** In addition, the GREAT Britain and Northern Ireland campaign will fund a £1 million campaign to promote the Scottish food and drink sector. This will include additional trade promotion to increase awareness and change perceptions of Scottish food and drink exports, including Scotch whisky. It will also expand tourism promotion campaigns to reach new markets.

**2.135 Western Gateway Independent Economic Review** – The government will support the Western Gateway, a strategic economic partnership across south Wales and the west of England, to oversee an independent economic review to identify long-term economic opportunities and challenges for the region.

**2.136 Support for Welsh language and broadcasting** – To support TV station S4C, which provides viewers with content in the Welsh language, the government will legislate to enable S4C to recover any VAT it pays in full.

## New technologies and support for innovation

**2.137 Step change in R&D investment** – The government will increase investment in science, innovation and technology to £22 billion by 2024-25.

**2.138 Leadership in key technologies** – The government will invest over £900 million to ensure UK businesses are leading the way in high-potential technology and sectors, including nuclear fusion, space, electric vehicles, and life sciences.

**2.139 High-risk research agency** – The UK will invest at least £800 million in a new blue skies research agency.

**2.140 Funding for world-leading research** – The government will invest up to £400 million extra in 2020-21 to support world-leading research, infrastructure and equipment across the UK.

**2.141 Mathematics research** – The government will invest £300 million between 2020-21 and 2024-25. This will increase funding available for new PhDs, fellowships and research projects.

**2.142 Specialist institutions** – The government will invest £80 million to support the UK's foremost specialist institutions. This includes organisations such as the London School of Hygiene and Tropical Medicine, the Royal College of Art and the Institute of Cancer Research, among others.

**2.143 Defence R&D** – The government will invest an additional £100 million in Defence R&D. This will develop capabilities in response to threats facing the UK, including funding for cutting-edge technology in aviation and space propulsion.

**2.144 National Security Strategic Investment Fund (NSSIF)** – The government will provide an additional £50 million to the NSSIF. As well as investing in leading UK-based venture capital funds, the government will expand the NSSIF programme to make direct investments, alongside private sector co-investors, into companies with advanced technologies that can contribute to the UK's longer term national and economic security. The British Business Bank will operate NSSIF direct investments through a new government company called British Technology Investments Ltd.

**2.145 Animal health science estate** – The government will invest £1.4 billion over 10 years in the animal health science infrastructure at Weybridge, enhancing the UK's science capability whilst protecting the nation from the increasing threats of current and emerging animal diseases.

**2.146 Government science capability** – To support cross-cutting strategic science capabilities, the government will provide an additional £2 million in 2020-21 to the Government Chief Scientific Adviser and the Government Office for Science.

**2.147 Natural History Museum research facility** – The Budget allocates £180 million capital funding for a new, state-of-the-art Collections, Research and Digitisation Centre for the Natural History Museum at Harwell Science, Technology and Innovation Campus in Oxfordshire. This new facility will be a world-leading centre for natural sciences research and international collaboration and will preserve this unique research collection for future generations.

**2.148 Materials Processing Institute** – The government will provide up to £22 million, subject to business case, to support research and innovation in the steel and metals sector through the Materials Processing Institute.

**2.149 Life Sciences Investment Programme** – The Budget provides the British Business Bank with £200 million for a new dedicated equity investment programme that, invested alongside private sector capital, is expected to enable £600 million of investment to support the UK's best health and life science innovations. The programme will support large-scale venture growth funds investing in life sciences companies and it will launch within a year.

**2.150 Making the most of knowledge assets** – The public sector holds around £150 billion of knowledge assets (intellectual property, tech, data and other intangibles).[9] The government wants to unlock more value from these assets and support innovation and productivity. The government will establish a fund to invest in innovative public sector ideas and a new unit to scout for and develop these opportunities. Public bodies are spread across the country and this support will help level-up regional innovation capability and networks outside of the South East. Further detail will be provided in a forthcoming report.

**2.151 Better use of economic data** – Improving methods for monitoring the economy has never been more important. The Budget announces a new fund of up to £5 million per year, to support the development of new economic data and its more innovative use.

---

[9] 'Measuring Intangible Capital in the Public Sector' SPINTAN, December 2016 www.spintan.net/spintan-data

## Enterprise and business support

**2.152 Enhanced local business support** – Supporting enterprise is an important part of the government's ambition to level up regions across the UK. To ensure that all businesses have access to high quality support and advice in their region, the government will: (29)

- invest £10 million to increase **Growth Hub**[10] capacity and provide a high-quality, core business advice and guidance offer across all 38 Growth Hubs
- invest £13 million to expand the British Library's network of Business and Intellectual Property Centres to 21 cities and 18 surrounding local library networks, providing entrepreneurs with business support, free access to market intelligence, IP workshops and one-to-one coaching

**2.153 SME productivity** – Industry-led initiatives have a valuable role in supporting small businesses to improve their productivity. The government will invest up to an additional £5 million in Be the Business to expand its national productivity campaign and further develop its digital tools and resources.

**2.154 Business support reform** – The government will use the CSR to make it easier for businesses to access the information and support that is relevant for them. As a first step, BEIS will lead the development of a digital service to provide businesses with tailored information about appropriate sources of support.

**2.155 Start-Up Loans** – The government will extend the funding of the British Business Bank's Start-Up Loans programme to the end of 2021-22, supporting up to 10,000 further entrepreneurs across the UK to access finance to start a business. The government will set out plans to expand the programme at the CSR.

**2.156 Access to growth capital for innovative businesses** – Since the 2017 Patient Capital Review, the government has announced substantial support for innovative businesses seeking access to long-term growth capital. To build on this, the Budget will provide the British Business Bank with the resources to make up to £200 million of additional investment in UK venture capital and growth finance in 2020-21.

**2.157 Prompt payment** – The government is continuing its efforts to ensure that small businesses are paid promptly. BEIS will shortly be publishing a consultation on the merits of strengthening the powers of the Small Business Commissioner (SBC), building on the success the SBC has had in resolving payment disputes.

**2.158 Tax guidance for self-employed people** – To make it easier for self-employed people to navigate the tax system, the government will launch new interactive online guidance for taxpayers with non-Pay As You Earn income this summer.

**2.159 Mortgage guidance for self-employed people** – The government will explore how to improve the guidance available for self-employed people applying for a mortgage.

**2.160 Support for self-employed parents** – The government will consider how to provide appropriate support to self-employed parents so that they can continue to run their businesses, as part of its wider review of Parental Pay and Leave.

**2.161 Direct Payments to farmers** – Last year the government announced £2.8 billion of funding for Direct Payments to farmers for 2020. This funding is spread over two financial years to provide flexibility for Defra and the devolved administrations, of which £2.7 billion falls in financial year 2020-21. (4)

[10] https://www.lepnetwork.net/growth-hubs/

## Trade and investment

**2.162 Digital Trade Network** – The Budget announces £8 million for DIT and DCMS to pilot a Digital Trade Network in the Asia Pacific region, helping innovative UK companies to access opportunities in key markets.

**2.163 UK Export Finance (UKEF) Direct Lending Facility** – UKEF offer loans to buyers of UK goods and services, particularly in emerging markets, to encourage them to buy from the UK. This lending has been capped at £3 billion with an additional £2 billion provided at Budget 2018 for use in 2020-21 and 2021-22 only. The Budget announces that UKEF will permanently retain this additional capacity as well as have a new £2 billion lending facility for projects supporting clean growth and a new £1 billion facility to support overseas buyers of UK defence and security goods and services.

**2.164 UKEF support for exporters** – To provide improved support for exporters in energy transition and clean growth sectors, UKEF will enhance its face-to-face support in the North of England and Scotland where energy supply chains are economically important.

**2.165 UKEF support for fixed rate finance** – UKEF will update its terms to allow it to better support export finance on a fixed-rate basis across its full product range, allowing customers to benefit from certainty of financing costs.

**2.166 Regional exports and investment** – DIT will drive investment into and end-to-end support for exporters from the Northern Powerhouse, the Midlands Engine and the Western Gateway through dedicated local champions based at key overseas posts.

**2.167 Advice for exporters** – DIT will increase its capacity to support exporters focused on the Northern Powerhouse, the Midlands Engine and the South West by increasing the number of international trade advisers available to provide personalised support to exporters.

**2.168 Enhanced market access support** – DIT will increase its resource and capability to identify and address market access barriers preventing UK exporters from accessing particular markets.

**2.169 British Film Commission** – The Budget allocates £4.8 million to expand the work of the British Film Commission to promote the UK as a destination of choice for studio space investment. The British Film Commission will act as a single source of expert advice for investors and developers and provide targeted support at the early stages of viable projects to facilitate increased provision of studio facilities across the UK.

**2.170 Start-up and Innovator visas** – DIT will become an endorsing body to allow it to directly support visa applications for eligible foreign investors seeking to start a business in the UK.

**2.171 Technical amendment to the process of import duty variation** – The government will legislate to amend section 15 of the Taxation (Cross-border Trade) Act 2018 by refining the criteria used to determine when the government may vary the amount of import duty in the context of an international trade dispute. This will allow the government to vary import duty where it considers this appropriate, having regard to relevant international agreements and obligations. The amendment will enable the UK to respond adequately to developments in the international trading system.

# Tax decisions

## Personal tax

**2.172 Increasing National Insurance thresholds** – The Budget confirms the government's commitment to increase the thresholds at which employees and the self-employed start paying National Insurance contributions (NICs) to £9,500 from April 2020.[11] Around 1.1 million people will be taken out of paying Class 1 and Class 4 NICs entirely.[12] This is the first step in meeting the government's ambition to increase these thresholds to £12,500, which would save a typical employee over £450 per year.[13] (12)

**2.173 Income tax and National Insurance exemptions for bursary payments to care leavers –** The government will legislate in Finance Bill 2020 to introduce an income tax exemption for the bursary paid by the Education and Skills Funding Agency to care leavers aged 16 to 24 who start an apprenticeship. Corresponding legislation will be introduced to mirror the income tax exemption for NICs. This legislation will confirm HMRC's current position that care leavers' bursaries are tax exempt, including those paid prior to the 2020-21 tax year.

**2.174 Increasing the flat rate deduction for homeworking –** The government will increase the maximum flat rate income tax deduction available to employees to cover additional household expenses from £4 per week to £6 per week where they work at home under homeworking arrangements. This will take effect from April 2020.

**2.175 Tax treatment of the Troubles Permanent Disablement Payment Scheme –** The government will legislate in Finance Bill 2020 to introduce income tax, inheritance tax and capital gains tax exemptions for payments made on or after May 2020 under the Troubles Permanent Disablement Payment Scheme.

**2.176 Tax treatment of social security benefits in Scotland –** The government will legislate in Finance Bill 2020 to clarify the income tax treatment of three new social security payments. The legislation will confirm that the following three benefits introduced by the Scottish government are exempt from income tax: Job Start; Disability Assistance for Children and Young People; and, the Scottish Child Payment. The legislation also includes a new power which permits the government to confirm by secondary legislation when new social security benefits introduced by the UK government or any of the devolved administrations will be tax exempt. The changes will take effect from April 2020.

**2.177 Tax treatment of the Windrush Compensation Scheme** – As announced in April 2019, the government will legislate in Finance Bill 2020 to introduce exemptions from income tax, inheritance tax and capital gains tax for payments made on or after 3 April 2019 under the Windrush Compensation Scheme. The legislation also includes a new power to exempt any necessary future compensation payments by statutory instrument from income tax, inheritance tax and capital gains tax, where appropriate. (64)

**2.178 Review of changes to the off-payroll working rules (commonly known as IR35)** – At Budget 2018 the government announced that it would reform the off-payroll working rules in the private and third sectors from April 2020. The government has recently concluded a review of the reform, and is making a number of changes to support its smooth and successful implementation. The government believes it is right to address the fundamental unfairness of the non-compliance with the existing rules, and the reform will therefore be legislated in Finance Bill 2020 and implemented on 6 April 2020, as previously announced.

[11] '31 million taxpayers to get April tax cut', HM Treasury, 30 January 2020.

[12] HMRC analysis based on Survey of Personal Incomes (SPI) 2017-18 data, and Budget 2020 OBR forecast.

[13] HM Treasury analysis, see 'Budget 2020 data sources'.

**2.179 National Insurance holiday for employers of veterans in first year of civilian employment** – To support the employment of veterans, the government is meeting the commitment to introduce a National Insurance holiday for employers of veterans in their first year of civilian employment. A full digital service will be available to employers from April 2022; however, transitional arrangements will be in place in the 2021-22 tax year which will effectively enable employers of veterans to claim this holiday from April 2021. The holiday will exempt employers from any NICs liability on the veteran's salary up to the Upper Earnings Limit. The government will consult on the design of this relief. (16)

**2.180 Tax treatment of welfare counselling provided by employers –** The government will extend the scope of non-taxable counselling services to include related medical treatment, such as cognitive behavioural therapy, when provided to an employee as part of an employer's welfare counselling services. The changes will take effect from April 2020.

**2.181 Top Slicing Relief (TSR) on life insurance policy gains** – Following a recent First-Tier Tribunal case, the government will legislate in Finance Bill 2020 to put beyond doubt the calculation of TSR by specifying how allowances and reliefs can be set against life insurance policy gains. This measure will apply to all relevant gains occurring on or after 11 March 2020. (49)

## Pensions and savings tax

### Pensions tax

**2.182 Call for evidence on pension tax administration –** Those earning around or below the level of the personal allowance and saving into a pension may benefit from a top-up on their pension savings equivalent to the basic rate of tax, even if they pay no tax. Whether they receive this top-up depends on how their pension scheme administers tax relief. The government has committed to reviewing options for addressing these differences and will shortly publish a call for evidence on pensions tax relief administration.

**2.183 Tapered annual allowance for pensions** – The pensions annual allowance is the maximum amount of tax-relieved pension savings that can be accrued in a year. For those on the highest incomes, the annual allowance tapers down from £40,000. HM Treasury has reviewed the tapered annual allowance and its impact on the NHS, as well as on public service delivery more widely.

**2.184** To support the delivery of public services, particularly in the NHS, the two tapered annual allowance thresholds will each be raised by £90,000. This means that from 2020-21 the "threshold income" will be £200,000, so individuals with income below this level will not be affected by the tapered annual allowance, and the annual allowance will only begin to taper down for individuals who also have an "adjusted income" above £240,000. (7)

**2.185** For those on the very highest incomes, the minimum level to which the annual allowance can taper down will reduce from £10,000 to £4,000 from April 2020. This reduction will only affect individuals with total income (including pension accrual) over £300,000. Proposals to offer greater pay in lieu of pensions for senior clinicians in the NHS pension scheme will not be taken forward. (7)

**2.186 Lifetime allowance for pensions –** The lifetime allowance, the maximum amount someone can accrue in a registered pension scheme in a tax-efficient manner over their lifetime, will increase in line with CPI for 2020-21, rising to £1,073,100.

## Savings tax

**2.187 Starting rate for savings tax band** – The band of savings income that is subject to the 0% starting tax rate will remain at its current level of £5,000 for 2020-21.

**2.188 Individual Savings Account (ISA) annual subscription limit** – The adult ISA annual subscription limit for 2020-21 will remain unchanged at £20,000. (55)

**2.189 Junior ISA and Child Trust Fund annual subscription limit** – The annual subscription limit for Junior ISAs and Child Trust Funds will be increased from £4,368 to £9,000.

# Business tax

## Employer NICs

**2.190 Increasing the Employment Allowance –** The government will increase the Employment Allowance from £3,000 to £4,000 from April 2020. This will benefit around 510,000 businesses by reducing their costs of employment, with an average gain of £850 per year.[14] The increase will take around 65,000 businesses out of paying NICs entirely and means the government will have doubled the value of the Employment Allowance in four years.[15] (25)

## Business rates

**2.191 Business rates retail discount** – The government has already announced that, for one year from 1 April 2020, the business rates retail discount for properties with a rateable value below £51,000 in England will increase from one third to 50% and will be expanded to include cinemas and music venues. To support small businesses in response to COVID-19 the retail discount will be increased to 100% and expanded to include hospitality and leisure businesses for 2021. (26)

**2.192 Business rates pubs discount** – The government previously committed to introducing a £1,000 business rates discount for pubs with a rateable value below £100,000 in England for one year from 1 April 2020. To further support pubs, in response to COVID-19 the discount for pubs will be increased to £5,000. (27)

**2.193 Business rates local newspaper office space discount** – The £1,500 business rates discount for office space used by local newspapers in England will be extended for an additional five years until 31 March 2025.

**2.194 Business rates public lavatories relief** – The government will bring forward legislation as soon as possible in this session to provide mandatory 100% business rates relief for standalone public lavatories in England from April 2020.

**2.195** Local authorities will be fully compensated for the loss of income as a result of these business rates measures.

**2.196 Business rates review** – The government is launching a fundamental review of business rates to report in the autumn. The Terms of Reference for this review are published alongside this Budget and a call for evidence will be published in the spring.

---

[14] HMRC analysis based on Pay As You Earn Real Time Information, the ONS Inter-Departmental Business Register and Open Geography Portal.

[15] HMRC analysis based on Pay As You Earn Real Time Information, the ONS Inter-Departmental Business Register and Open Geography Portal.

**2.197 Valuation Office Agency (VOA) business systems transformation programme** – The government will invest an additional £11.5 million in the VOA in 2020-21 to support the modernisation of VOA systems and processes, to increase efficiency and improve customer service in the future.

## Enterprise tax

**2.198 Capital Allowances: Structures and buildings allowance (SBA) rate** – The annual rate of capital allowances available for qualifying investments to construct new, or renovate old, non-residential structures and buildings will increase from 2% to 3%. The change will take effect from 1 April 2020 for corporation tax and 6 April 2020 for income tax. The introduction of SBA at Budget 2018 greatly enhanced the international competitiveness of the UK's tax system and this increased rate of relief goes even further, providing businesses who invest with over £1 billion in additional relief by the end of 2024-25. (23)

**2.199 Capital Gains Tax: Reduction in the Entrepreneurs' Relief lifetime limit** – From 11 March 2020, the lifetime limit on gains eligible for Entrepreneurs' Relief (which offers a reduced 10% rate of Capital Gains Tax on qualifying disposals) will be reduced from £10 million to £1 million, in response to evidence that it has done little to incentivise entrepreneurial activity and that most of the benefit accrues to a small number of very affluent taxpayers.[16] This will help ensure that the tax system is fair and sustainable while leaving over 80% of those using the relief unaffected.[17] (46)

**2.200 Review of Enterprise Management Incentives (EMI) scheme** – The government will review the EMI scheme to ensure it provides support for high-growth companies to recruit and retain the best talent so they can scale up effectively, and examine whether more companies should be able to access the scheme.

**2.201 Research & Development Expenditure Credit (RDEC) rate** – The rate of RDEC will increase from 12% to 13% from 1 April 2020, supporting businesses investing in R&D and helping to drive innovation in the economy. (24)

**2.202 Consultation on R&D tax credit qualifying costs** – The government will consult on whether expenditure on data and cloud computing should qualify for R&D tax credits.

**2.203 Preventing abuse of the R&D relief for small and medium-sized enterprises: Summary of responses and consultation** – Following consultation last year, the introduction of the PAYE cap on the payable tax credit in the SME R&D schemes will be delayed until 1 April 2021. The government has listened to industry and will also consult on changes to the cap's design, to ensure it targets abusive behaviour as intended while ensuring that eligible businesses are able to access the relief. (60)

## Corporate tax

**2.204 Corporation tax (CT) rate** – Since 2010 the government has cut the headline rate of CT from 28% to 19%, giving the UK the lowest headline rate in the G20.[18] To provide support for vital public services while maintaining the UK's competitive rate of CT, the government will legislate to retain the current 19% rate in April 2020. (45)

**2.205 Digital services tax (DST)** – As announced at Budget 2018, the government will introduce a new 2% tax on the revenues certain digital businesses earn from 1 April 2020. This will ensure the amount of tax paid in the UK reflects the value these businesses derive from their interactions with, and the contributions of, an active user base. Legislation will require

---

[16] Internal HMRC analysis of Entrepreneurs' Relief data.

[17] 'Capital Gains Tax Entrepreneurs' Relief: Behaviours and Motivations', IFF Research, May 2017

[18] 'Corporate tax rates table', KPMG, 2019

businesses to pay the DST on an annual basis, consistent with the draft legislation published in July 2019. The government will continue to give consideration to how the legislation applies to marketplace delivery fees and whether that application is consistent with the policy rationale of the DST. The government remains committed to developing a multilateral solution to the challenges digitalisation has created for the corporate tax system and will repeal the DST once an appropriate global solution is in place. (50)

**2.206 Intangibles reform** – The government will legislate in Finance Bill 2020 to remove the pre-2002 exclusion from the Intangible Fixed Assets (IFA) regime to support UK investment in intellectual property and other intangible assets. This means tax relief for the cost of acquiring corporate intangible assets on or after 1 July 2020 will be provided under a single regime, subject to restrictions to prevent tax avoidance. (28)

**2.207 Corporate capital loss restriction** – As announced at Budget 2018, from 1 April 2020, the government will restrict the proportion of annual capital gains that can be relieved by brought-forward capital losses to 50%. This measure includes an allowance that gives companies unrestricted use of up to £5 million capital or income losses each year, meaning that 99% of companies will be unaffected.[19] Following consultation on the detailed design of the rules,[20] the government will also exclude certain companies in liquidation from the scope of the restriction. (51)

**2.208 Review of the UK funds regime** – The government will undertake a review of the UK's funds regime during 2020. This will cover direct and indirect tax, as well as relevant areas of regulation, with a view to considering the case for policy changes. The review will begin with a consultation, to be published at the Budget, on whether there are targeted and merited tax changes that could help to make the UK a more attractive location for companies used by funds to hold assets. The review will also consider the VAT treatment of fund management fees and other aspects of the UK's funds regime.

**2.209 Transfer of unlisted securities to connected companies for Stamp Duty and Stamp Duty Reserve Tax** – In Finance Act 2018-19, the government introduced a targeted market value rule to prevent artificial reduction of the tax due on share acquisitions when listed shares are transferred to a connected company. This rule is being extended to unlisted shares in Finance Bill 2020 to prevent further tax avoidance. As part of this change, the government will amend legislation to prevent a double tax charge arising on certain company reorganisations. (67)

**2.210 Consultation on the tax impact of the withdrawal of the London Inter-Bank Offered Rate (LIBOR)** – The government will consult to ensure that where tax legislation makes reference to LIBOR it continues to operate effectively. The consultation will also enable the government to ensure it is aware of all the significant tax issues that arise from the reform of LIBOR and other benchmarks.

**2.211 Consultation on aspects of the hybrid mismatch rules** – The government will publish a consultation on the corporation tax rules that apply to hybrid mismatch arrangements that seek to exploit the differences in tax treatment between two jurisdictions. The consultation seeks to ensure that the hybrid mismatch rules work proportionately and as intended.

---

[19] Internal HMRC analysis

[20] 'Corporate Capital Loss Restriction: consultation on delivery', HM Treasury and HM Revenue & Customs, July 2019.

## Property tax

**2.212 Non-UK resident Stamp Duty Land Tax (SDLT) surcharge** – The government will introduce a 2% SDLT surcharge on non-UK residents purchasing residential property in England and Northern Ireland from 1 April 2021. This will help to control house price inflation and to support UK residents to get onto and move up the housing ladder. The money raised from the surcharge will be used to help address rough sleeping. (47)

**2.213 Housing co-operatives: Annual Tax on Enveloped Dwellings (ATED) and Stamp Duty Land Tax (SDLT)** – To make the taxation of housing co-operatives fairer, the government will introduce a relief for qualifying housing co-operatives from the ATED and the 15% flat rates of SDLT on purchases of dwellings over £500,000. The SDLT relief in England and Northern Ireland will take effect from Autumn Budget 2020 and the UK-wide ATED relief from 1 April 2021 with a refund available for 2020-21.

## Energy and environmental tax

**2.214 Plastic Packaging Tax** – As announced at Budget 2018 and following consultation in spring 2019,[21] the government will introduce a new Plastic Packaging Tax from April 2022 to incentivise the use of recycled plastic in packaging. The Budget sets the rate at £200 per tonne of plastic packaging that contains less than 30% recycled plastic. This will apply to the production and importation of plastic packaging. The government will keep the level of the rate and threshold under review to ensure that the tax remains effective in increasing the use of recycled plastic. The government will also extend the scope of the tax to the importation of filled plastic packaging and apply a minimum threshold of 10 tonnes of plastic packaging to ensure the smallest businesses are not disproportionately impacted. The Budget also announces the launch of a further consultation on the detailed design and implementation of the tax, which includes consideration of an exemption for certain types of medical packaging. (38)

**2.215 Aggregates Levy** – The government will freeze the Aggregates Levy rate in 2020-21 and will be publishing a summary of responses and government next steps to last year's comprehensive review of the levy. (52)

**2.216 Increasing the gas rates under the Climate Change Levy (CCL) for years 2022-23 and 2023-24** – To meet the UK's net zero commitment, the UK must continue to remove incentives to choose gas over electricity, which is a cleaner energy source. Building on the Budget 2016 announcement to make gas and electricity rates equal by 2025, the government is raising the rate on gas to £0.00568/kWh in 2022-23 and to £0.00672/kWh in 2023-24 whilst freezing the rates on electricity. To ensure the tax system treats fuels that are used off the gas grid more equitably, the government will freeze LPG at 2019-20 levels until April 2024. (41)

**2.217 Extending the Climate Change Agreement (CCA) scheme** – To support energy-intensive businesses to operate in a more environmentally sustainable way, the government will reopen and extend the CCA scheme by two years. The CCA scheme allows businesses to reduce their CCL bill in exchange for meeting targets to improve their energy efficiency. The terms of the extended scheme will be set out in a consultation to be launched shortly after Budget. As part of this, the government will simultaneously consult on long-term options for the CCA scheme.

**2.218 Carbon price support (CPS) rate** – The government will freeze the rate of the CPS at £18t/$CO_2$e in 2021-22. Alongside wider carbon pricing policies, this will continue to encourage decarbonisation of the power sector. (43)

[21] 'Plastic packaging text', HM Treasury, July 2019.

**2.219 Carbon pricing after the transition period** – The UK will continue to apply an ambitious carbon price from 1 January 2021 to support progress towards reaching net zero. The government will legislate at Finance Bill 2020 to prepare for a UK Emissions Trading System (ETS), which could be linked to the EU ETS. The government will also legislate for a carbon emissions tax as an alternative carbon pricing policy and consult on the design of a tax in spring 2020.

## Transport taxes

**2.220 Fuel duty** – The government will freeze fuel duty for a tenth year in a row, cumulatively saving the average car driver £1,200 compared to the pre-2010 escalator.[22] Future fuel duty rates will be considered alongside measures that are needed to help meet the UK's net zero commitment. (13)

**2.221 Air Passenger Duty (APD) rates** – APD rates will increase in line with RPI for 2021-22, meaning that short haul rates remain frozen at £13, benefitting 80% of passengers.[23] The rate for long haul economy will increase by £2, and the rates for those travelling in premium economy, business and first class will increase by £4. Those travelling long-haul by private jets will see the rate increase by £13.

**2.222 Aviation tax reform** – In January 2020 the government announced that it would undertake a review of APD ahead of the Budget to ensure that regional connectivity is supported while meeting the UK's commitment to net zero emissions by 2050. As a result, the government will consult on aviation tax reform in spring 2020. The government will consider the case for changing the APD treatment for domestic flights, such as reintroducing a return leg exemption, and for increasing the number of international distance bands.

**2.223 Vehicle Excise Duty (VED): Rates** – The government will uprate VED rates for cars, vans and motorcycles in line with RPI from 1 April 2020. To support the haulage sector, the government will freeze HGV VED and the HGV Road User Levy for 2020-21. (53)

**2.224 VED: Zero emission vehicles (ZEVs)** – From 1 April 2020, the government will exempt all ZEVs registered until 31 March 2025 from the VED 'expensive car' supplement. The measure will incentivise the uptake of ZEVs to support the phasing out of petrol and diesel vehicles. (44)

**2.225 VED: Motorhomes** – From 12 March 2020, the government will reduce annual VED liabilities for most new motorhomes to a flat rate of £265, which will rise to £270 for 2020-21, as motorhome manufacturers and dealers will not be required to provide a $CO_2$ emissions figure when registering new motorhomes with the Driver and Vehicle Licensing Agency. From 1 April 2021, the government will align the VED treatment of new motorhomes and vans. (18)

**2.226 Call for evidence on VED** – The government is publishing a call for evidence which will include how VED can be used to support the take-up of zero and ultra-low emission vehicles and reduce overall emissions from road vehicles.

**2.227 Company car tax (CCT): Rates** – As set out in July 2019,[24] the government will reduce most CCT rates by 2% in 2020-21 for cars first registered from 6 April 2020. Rates will return to planned levels over the following two years, increasing by 1% in 2021-22 and 1% in 2022-23. Rates will then be frozen until 2024-25. (66)

[22] HM Treasury calculations.
[23] HM Treasury calculations based on 'Air Passenger Duty Bulletin', HMRC, September 2019.
[24] 'Review of WLTP and vehicle taxes: summary of responses', HM Treasury, July 2019.

**2.228 Van benefit charge nil-rating for zero emission vans** – From April 2021, the government will apply a nil rate of tax to zero-emission vans within van benefit charge. This measure will save businesses an estimated £433 per van in tax in 2021-22.[25]

**2.229 Company vehicles** – From 6 April 2020, fuel benefit charges and the van benefit charge will increase in line with CPI. (54)

**2.230 First year allowances for business cars from April 2021** – To support the uptake of zero emission vehicles (ZEVs) and ultra-low emission vehicles (ULEVs), from April 2021, the government will extend first year allowances to ZEVs only and apply the main rate writing down allowance (WDA) of 18% to cars with emissions up to 50g/km. The special rate WDA of 6% will apply to higher polluting cars with emissions above 50g/km. First year allowances for zero emission goods vehicles and natural gas and hydrogen refuelling equipment will also be extended. (42)

**2.231 Red diesel: Removing entitlement** – The government will remove entitlement to the use of red diesel and rebated biofuels from April 2022, except for agriculture (including horticulture, pisciculture and forestry), rail and for non-commercial heating (including domestic heating). The government will consult on whether the entitlement to use red diesel and rebated biofuels is justified for any other users, for example there is a strong case for continued use by ferries carrying paid passengers on the UK's rivers and inland waterways, or public entertainment. Commercial boats on open waters, including ferries and fishing boats, will remain entitled to the Marine Voyages Relief so will not have to pay more for their fuel. This measure will incentivise businesses to improve the energy efficiency of their vehicles and machinery or look for greener alternatives. To support the development of alternatives that these businesses can switch to, the Budget has also committed to at least doubling the size of the energy innovation programme, accelerating the design and production of innovative clean energy technologies. (39)

**2.232 Red diesel: Prohibition of use for propelling private pleasure craft** – Private pleasure craft already pay the standard white diesel rate for propulsion. They will still be entitled to use red diesel for their heating use. Where they have one tank for propulsion and heating, the government will explore options that prevent them from having to pay a higher rate of duty on their heating use than they would otherwise have to pay. Details on the implementation of this power will be set out in due course.

## VAT

**2.233 VAT on e-publications** – The Government will introduce legislation to apply a zero rate of VAT to e-publications from 1 December 2020, to make it clear that e-books, e-newspapers, e-magazines and academic e-journals there are entitled to the same VAT treatment as their physical counterparts. (15)

**2.234 VAT Postponed Accounting** – From 1 January 2021 postponed accounting for VAT will apply to all imports of goods, including from the EU. This will provide an important boost to those VAT registered UK businesses which are integrated in international supply chains as they adapt to the UK's position as an independent trading nation.

**2.235 Abolition of tampon tax** – From 1 January 2021 the government will use freedom from EU law to enable a zero rate of VAT to be charged on women's sanitary products. (17)

**2.236 Long-term passengers' policy consultation** – The government is publishing a consultation alongside Budget to gather views on the potential approach to duty- and tax-free goods policy after the transition period following the UK's departure from the EU.

---

[25] HM Treasury analysis, see 'Budget 2020 data sources'.

**2.237 Long-term cross-border goods policy** – The government will launch an informal consultation over spring 2020 on the VAT and excise treatment of goods crossing UK borders after the EU exit transition period.

**2.238 VAT on fund management** – As announced on 4 March 2020[26] the government is legislating to clarify when fund management services are exempt from VAT.

**2.239 VAT on financial services** – The government will set up an industry working group to review how financial services are treated for VAT purposes.

**2.240 VAT Quick Fixes Directive** – The government will introduce legislation to introduce simplified rules for the VAT treatment of intra-EU movements of call-off stock, allowing businesses to delay accounting for VAT until the goods are called-off. The legislation will apply to goods which are removed from a Member State on or after 1 January 2020 (sic).

**2.241 VAT Partial Exemption** – Following the recent call for evidence on the simplification of the VAT rules on Partial Exemption and the Capital Goods Scheme,[27] the government will continue to engage with stakeholders in relation to their responses and will publish a response in due course.

## Alcohol, tobacco and other duties

**2.242 Alcohol duty rates** – Duty rates on beer, spirits, wine and cider will be frozen. (14)

**2.243 Post-EU exit alcohol review** – The government recognises the complexity of the current duty system and will review potential reforms to be implemented after the transition period, beginning by publishing a call for evidence by the summer.

**2.244 Small Brewers' Relief (SBR)** – The government will publish the results of our review into Small Brewers Relief in the spring.

**2.245 Tobacco duty rates** – Duty rates on all tobacco products will increase by RPI + 2% until the end of this Parliament. The rate on hand-rolling tobacco will increase by RPI + 6% this year. These changes will take effect from 6pm on 11 March 2020. (48)

**2.246 Gaming Duty** – The government will legislate in Finance Bill 2020 to raise the Gross Gaming Yield (GGY) bandings for Gaming Duty in line with inflation. The revised bandings must be used for accounting periods starting on or after 1 April 2020.

## Avoidance, evasion and non-compliance

**2.247** Since 2010 the government has secured and protected over £200 billion of tax that would have otherwise gone unpaid.[28] The Budget builds on this work and announces further action to tackle tax avoidance, evasion and other forms of non-compliance that will raise an additional £4.7 billion between now and 2024-25.

**2.248 Preventing the illicit trade of tobacco** – The government is announcing increased resources for Trading Standards and HMRC to combat the illicit tobacco trade, including the creation of a UK-wide HMRC intelligence sharing hub. The government will also consult on proposals for stronger penalties for tobacco tax evasion.

---

[26] 'Value Added Tax (Finance) Order 2020', UK Statutory Instruments, March 2020.

[27] 'Call for evidence: simplification of partial exemption and the Capital Goods Scheme', HM Revenue & Customs, July 2019

[28] 'Annual Report and Accounts 2018-19, HMRC, August 2019; 'Spring Statement 2019: Written Ministerial Statement', HM Treasury, March 2019

**2.249 Tackling Construction Industry Scheme (CIS) abuse** – The government will legislate to prevent non-compliant businesses from using the CIS to claim tax refunds to which they are not entitled. The government is also publishing a consultation which introduces options on how to promote supply chain due diligence. (57)

**2.250 Domestic reverse charge for building and construction services** – As announced in September 2019,[29] the implementation of the VAT domestic reverse charge for building and construction services, which prevents losses through so-called 'missing trader' fraud, will be delayed until 1 October 2020. (68)

**2.251 VAT Agricultural Flat Rate Scheme (AFRS)** – Following informal consultation with stakeholders in 2019 the government will introduce new entry and exit rules for the AFRS.

**2.252 Conditionality: Hidden economy** – The government will legislate in Finance Bill 2020-21 to make the renewal of licenses to drive taxis and private hire vehicles (PHVs, e.g. minicabs), operate PHV firms, and deal in scrap metal conditional on applicants completing checks that confirm they are appropriately registered for tax. This measure will make it more difficult for non-compliant traders to operate in the hidden economy and help level the playing field for the compliant majority. These changes will take effect in England and Wales in April 2022. The government is considering extending this reform to Scotland and Northern Ireland in the future and will work with the devolved administrations to this effect. (58)

**2.253 Conditionality**: **Wider application** – The government will publish a discussion document seeking views on the wider application of tax conditionality in the spring. Tax conditionality refers to a principle whereby businesses are granted access to government awards and authorisations (such as approvals, licenses, grants) only if they are able to demonstrate good tax compliance.

**2.254 Additional compliance resources for HMRC** – The government is investing in additional compliance officers and new technology for HMRC. This investment is forecast to bring in £4.4 billion of additional tax revenue up to 2024-25 by enabling HMRC to further reduce the tax gap through additional compliance activity and expanding debt collection capabilities.[30] (59)

## Response to the Loan Charge Review

**2.255 Response to the independent Loan Charge Review** – The Budget confirms the government's response to Sir Amyas Morse's Independent Loan Charge Review[31] and sets out the Exchequer costs of accepting the recommendations. These will be legislated for in the forthcoming Finance Bill. To implement the changes, the government will also provide HMRC with additional operational funding. However, disguised remuneration schemes continue to be used. Therefore, the government will shortly issue a call for evidence on further action to stamp out these schemes. (63)

**2.256 Tackling promoters of tax avoidance** – As announced in the government's response to the independent Loan Charge Review,[32] the government will legislate in Finance Bill 2020-21 to take further action against those who promote and market tax avoidance schemes. The legislation, which will take effect following Royal Assent, will:

- allow HMRC to obtain information about the enabling of abusive schemes as soon as they are identified by strengthening information powers for HMRC's existing regime to tackle enablers of tax avoidance schemes

[29] 'Revenue and Customs Brief 10 (2019): domestic reverse charge VAT for construction services – delay in implementation', HM Revenue & Customs, September 2019.

[30] HM Treasury internal estimate using HMRC data.

[31] 'Disguised remuneration: independent loan charge review', HM Treasury and HM Revenue & Customs, December 2019.

[32] 'Disguised remuneration: independent loan charge review', HM Treasury and HM Revenue & Customs, December 2019.

- ensure enabler penalties are felt without delay for multi-user schemes, meaning anyone enabling tax avoidance arrangements that are later defeated will face a penalty of 100% of the fees they earn
- enable HMRC to act promptly where promoters fail to provide information on their avoidance schemes. In particular, these changes will help HMRC obtain the information needed to bring a scheme into the Disclosure of Tax Avoidance Schemes regime and empower HMRC to act faster where avoidance schemes are being promoted
- equip HMRC to more effectively stop promoters from marketing and selling avoidance schemes as early as possible
- ensure promoters fulfil their obligations under the Promoters of Tax Avoidance Scheme (POTAS) regime, including where they have tried to abuse corporate structures to get around the rules
- make further technical amendments to the POTAS regime, including preventing spurious legal challenges from disrupting the process of scrutinising promoters, so the regime can continue to operate effectively
- make additional changes to the General Anti-Abuse Rule (GAAR) so it can be used as intended to tackle avoidance using partnership structures

**2.257 HMRC's promoter strategy** – On top of the legislative changes the government will introduce in Finance Bill 2020-21, HMRC will publish a new ambitious strategy for tackling the promoters of tax avoidance schemes. This will outline the range of policy, operational and communications interventions both underway and in development to drive those who promote tax avoidance schemes out of the market, disrupt the supply chain to stop the spread of marketed tax avoidance, and deter taxpayers from taking up the schemes.

**2.258 Raising standards in the market for tax advice** – The government will publish a call for evidence in the spring on raising standards for tax advice. This will seek evidence about providers of tax advice, current standards upheld by tax advisers, and the effectiveness of the government's efforts to support those standards, in order to give taxpayers more assurance that the advice they are receiving is reliable.

## Tax administration

**2.259 Future of Making Tax Digital** – The government will publish an evaluation of the introduction of Making Tax Digital for VAT, along with related research.

**2.260 Large business notification** – From April 2021 large businesses will be required to notify HMRC when they take a tax position which HMRC is likely to challenge. This policy will draw on international accounting standards which many large businesses already follow. The government will consult shortly on the detail of the notification process. (56)

**2.261 Protecting your taxes in insolvency** – As announced at Budget 2018, the government will change the rules so that when a business enters insolvency, more of the taxes paid in good faith by its employees and customers and temporarily held in trust by the business go as intended to fund public services, rather than being distributed to other creditors. The Budget delays the commencement date of this measure from 6 April to 1 December 2020 and extends this measure to Northern Ireland. This reform will only apply to taxes collected and held by businesses on behalf of other taxpayers (VAT, PAYE income tax, employee NICs and CIS deductions). The rules will remain unchanged for taxes owed by businesses themselves, such as corporation tax and employer NICs. The legislation will be introduced in Finance Bill 2020. (65)

**2.262 Clarifying the treatment of Limited Liability Partnership (LLP) returns** – The government will legislate prospectively and retrospectively in Finance Bill 2020 to put beyond doubt that LLPs should be treated as general partnerships under income tax rules. This will ensure HMRC can continue to amend LLP members' tax returns where the LLP operates without a view to profit. This measure does not create any new or additional obligations or liabilities for taxpayers. It clarifies the legislation to ensure the rules work as designed and intended.

**2.263 HMRC automation** – As announced on 31 October 2019,[33] the government will legislate to confirm that HMRC may use automated processes to issue taxpayers with notices to file tax returns and penalty notices. This measure will apply prospectively and retrospectively to put beyond doubt that the rules work as designed and intended. This does not create any new or additional obligations or liabilities for taxpayers.

**2.264 Insurance Premium Tax (IPT) call for evidence** – The government will shortly publish a summary of responses to the recent call for evidence on the operation of IPT,[34] along with information on a forthcoming consultation setting out the next stage in reforming how IPT operates.

**2.265 Funding HMRC to prepare for breathing space** – The government will invest an additional £12.5 million in HMRC in 2020-21 to begin work immediately on the implementation of breathing space. From early 2021 this will mean that those in problem debt can access a 60-day breathing space, including for debts to HMRC, while they engage with debt advice and work towards a sustainable debt solution.

## Competition and regulation

**2.266 Boosting competition in the digital and wider economy** – The government will accept all six of the Furman Review's[35] strategic recommendations for unlocking competition in digital markets. The government will consult on these in due course. A new cross-regulator taskforce, based in the Competition and Markets Authority (CMA), will report to the government within six months on a pro-competitive regime for digital platform markets. This will include advice on implementing a pro-competitive code of conduct for digital platforms with strategic market power. The government will also look at existing domestic or EU derived regulations that might hinder digital competition and entrench monopoly behaviours and will ensure that regulatory reforms applying to digital and tech businesses are pro-innovation and coherent.

**2.267 Reforming Regulation Initiative** – Good regulation is essential to successful businesses. The government will strive to achieve the right balance between supporting excellent business practice and providing protections for people and the environment. The Budget announces that BEIS is launching the Reforming Regulation Initiative. This will invite ideas from business and the public for regulatory reform in order to ensure that regulation is sensible and proportionate now that the UK has left the EU, and that the interests of small businesses are taken into account.

**2.268 Regulators' Pioneer Fund** – The government will launch a second round of the Regulators' Pioneer Fund, building on the success of the first round which was launched at Autumn Budget 2017. This £10 million of funding will enable regulators to unlock the potential of emerging technologies and help businesses to develop innovative products and services.

[33] 'HM Revenue and Customs Update: Written Statement – HCWS61', House of Commons, October 2019.
[34] 'Call for evidence: the operation of Insurance Premium Tax', HM Revenue & Customs, June 2019.
[35] 'Unlocking digital competition, Report of the Digital Competition Expert panel', HM Treasury, March 2019

**2.269 Financial Services Bill** – The Financial Services Bill will provide long-term market access between the UK and Gibraltar for financial services firms following EU exit, support a vibrant asset management industry by simplifying the process for overseas investment funds seeking to market into the UK and enable the implementation of the remaining Basel banking standards and a more proportionate prudential regime for investment firms. The government has published further details alongside Budget ahead of legislating later in the session. As a result of the proposed changes to the prudential regime for investment firms, the government will be taking steps to ensure that bank tax legislation continues to operate in line with current policy.

**2.270 Regulatory Coordination** – The Financial Services Future Regulatory Framework Review was announced at Mansion House 2019, with the first phase launching a call for evidence on regulatory coordination in July. The government is publishing a response to the call for evidence alongside Budget and setting out the next steps in the review. This response announces a new forum, bringing together government and regulators, to provide industry with a forward-look of upcoming regulatory initiatives. This forum will be made up of the Bank of England, Prudential Regulation Authority, Financial Conduct Authority (FCA), Payment Systems Regulator and Competition and Markets Authority, with HM Treasury as an observer member.

**2.271 Access to cash legislation** – The government will bring forward legislation to protect access to cash for those who need it. This will ensure industry continues to meet the changing needs of cash users.

**2.272 Regulation of pre-paid funeral plans** – The government is publishing the response to its consultation on the regulation of pre-paid funeral plans and will legislate to bring funeral plan providers within the remit of the FCA. This will protect consumers by ensuring, for the first time, that all pre-paid funeral plan providers are subject to robust regulation.

**2.273 Changes to the Credit Unions Act** – The government will bring forward legislation to allow credit unions to offer a wider range of products and services to their members, supporting their vital role in financial inclusion.

**2.274 Fintech review and delivery panel** – The government has invited Ron Kalifa OBE to lead a major review into the fintech sector. The review will identify what more industry and government can do to support growth and competitiveness, to ensure that the UK maintains its global leadership in this vital sector. The government will also extend funding for the Fintech Delivery Panel, as well as touring the regions and nations of the UK to showcase its diverse range of fintech firms.

**2.275 Digital currencies discussion paper** – The government looks forward to the publication of the Bank of England's discussion paper on a possible UK central bank digital currency (CBDC). The UK will continue to take a leading role in exploring digital currencies, and the wide-ranging opportunities and challenges they could bring.

**2.276 Cryptoassets consultation** – To protect consumers and support innovation in cryptoassets, the government intends to consult on a measure to bring certain cryptoassets into scope of financial promotions regulation. The government also intends to consult later in 2020 on the broader regulatory approach to cryptoassets, including new challenges from so-called 'stablecoins'.

**2.277 Call for evidence for the Payments Landscape Review** – In light of rapid technology developments, HM Treasury, working alongside the regulators and the Financial Policy Committee, is leading a Payments Landscape Review to make sure the UK's payments infrastructure and regulation are keeping pace. As part of this, HM Treasury will shortly be publishing a call for evidence to ask what more could be done by the government, industry and regulators to support a more innovative and resilient payments system and ensure the UK payments sector remains world leading.

**2.278 Open finance for SMEs** – In order to realise the vision for truly open finance, in which SMEs can share their data at the touch of a button, making it faster and easier to shop around for credit, HM Treasury will convene a summit with those at the cutting edge of industry innovation to establish what further data needs to be opened up.

**2.279 Digital Identity Unit** – The government will work to create a digital identity market that makes it possible for people to prove things about themselves without showing paper documents. This will help make opening a bank account, claiming benefits or buying a house simpler, safer and quicker. More secure and cost-effective online transactions will also boost business and the digital economy.

**2.280 Affordable Credit Challenge Fund** – By harnessing the UK's world-leading fintech expertise, this £2 million challenge fund promotes the development of innovative tech solutions that improve awareness and access to affordable lenders as an alternative to high cost credit. The winners of the challenge are Fair for You with EML and Lending Metrics, Police Credit Union with Credit Kudos, and Capital Credit Union with Nivo and Soar who will each receive £200,000 to further develop and scale their solutions.

## Financial transactions, asset sales and other decisions

**2.281 Royal Bank of Scotland** – The government intends to fully dispose of its Royal Bank of Scotland shareholding, subject to market conditions and achieving value for money for taxpayers. The government expects the programme of sales to be completed by 2024-25.

**2.282 UK Asset Resolution (UKAR)** – UKAR's balance sheet has reduced from £115.8 billion in 2010 to £8 billion following the latest sale of assets.[36] The government expects to return UKAR's subsidiaries Bradford & Bingley (B&B), NRAM Ltd[37] and their remaining assets to private ownership in 2020, subject to achieving value for money and market conditions remaining supportive.

**2.283** In May 2019, the government transferred sponsorship of B&B's and NRAM Ltd's pension schemes to UKAR in preparation for B&B and NRAM Ltd being returned to private ownership. The government intends, subject to securing the necessary parliamentary time, to create a new central government pension scheme for the members of the B&B and NRAM schemes. Members' pensions will not be affected by this transfer. Following the establishment of a new central government pension scheme, the government intends to sell assets held by the NRAM and B&B schemes over 2023-24 and 2024-25, subject to the necessary legislation being brought forward, supportive market conditions and achieving value for money.

**2.284 Student loan sale** – In December 2018, the government completed the second in its programme of sales of pre-2012 income-contingent student loans, expected to raise £15 billion by 2022-23. The sale raised £1.9 billion, reducing PSND and achieving value for money. Following an internal review, which was published at Budget, the government has decided not to pursue additional sales of pre-2012 income-contingent student loans.

**2.285** The government continues to explore options for the sale of wider corporate and financial assets, where there is no longer a policy reason to retain them and when value for money can be secured for taxpayers.

**2.286 Retail Prices Index consultation** – Alongside the Budget, the government and UK Statistics Authority (UKSA) are launching a consultation, announced on 4 September 2019,[38] on UKSA's proposal to address the shortcomings of the Retail Prices Index (RPI) measure

[36] https://www.gov.uk/government/news/loans-sale-to-return-49-billion-to-uk-taxpayers
[37] NRAM Ltd was formerly part of Northern Rock.
[38] 'Letter from Savid Javid, former Chancellor of the Exchequer', HM Treasury, September 2019.

of inflation. The consultation will cover, among other things, the issue of timing, including whether the UKSA's proposal might be implemented at a date other than 2030, and if so, when between 2025 and 2030, and issues on technical matters concerning the implementation of its proposal. The consultation will be open for a period of six weeks, closing on 22 April 2020. The government and UKSA will respond to the consultation before the Parliamentary summer recess.

**2.287 MPC remit** – The Chancellor is responsible for setting the MPC's remit. In the Budget, the Chancellor reaffirms the symmetric inflation target of 2% for the 12-month increase in the CPI measure of inflation. This target applies at all times.[39] The Chancellor also confirms that the Asset Purchase Facility (APF) will remain in place for the financial year 2020-21.

**2.288 Balance Sheet Review** – The government manages assets worth £2 trillion alongside £4.6 trillion of liabilities on behalf of citizens.[40] The Balance Sheet Review (BSR) was launched in 2017 to identify opportunities to dispose of assets that no longer serve a policy purpose, improve returns on retained assets, and reduce the risk and cost of liabilities. This work aims to put the UK at the forefront of the international drive to reduce waste and deliver improvements in the cost-effective management of public wealth, as recognised by the IMF in its October 2018 Fiscal Monitor. The BSR will conclude and report at this year's Comprehensive Spending Review.

**2.289** The government is exposed to £192 billion of contingent liabilities, including guarantees and insurance provided to the private sector.[41] The BSR has developed proposals to improve the management of these liabilities and address a key balance sheet risk recognised by the OBR in its July 2019 Fiscal Risk Report.[42] The government is publishing a report alongside Budget: 'Government as insurer of last resort' providing more detail on the policy approach.

[39] 'Monetary policy remit: Budget 2020', HM Treasury, March 2020.

[40] 'Whole of Government Accounts 2017 to 2018'; HM Treasury; May 2018.

[41] 'Whole of Government Accounts 2017 to 2018'; HM Treasury; May 2018.

[42] 'Fiscal Risks Report 2019', OBR, July 2019

# Chapter 3
# Quality of public finances

The government's significant progress in restoring the public finances to health over the last decade means it can now afford to support the economy in the short-term while investing to support long-term growth.

At Spending Round 2019, the government increased departmental spending by 4.1% in real terms between 2019-20 and 2020-21 delivering the fastest planned growth in day-to-day departmental spending in 15 years.

Government spending as a share of GDP will rise from 39.8% in 2019-20 to 40.7% in 2024-25. The average annual real growth rate of Total Managed Expenditure (TME), the total amount of money that the government spends through departments, local authorities, other public bodies and social security, will be 1.9% between 2019-20 and 2024-25.

The following tables are taken directly from Spring Budget 2020. Table 3.A sets out the path for Total Managed Expenditure (TME) to 2024-25.

## Total Managed Expenditure (in £ billion, unless otherwise stated)[1,2]

| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|
| CURRENT EXPENDITURE | | | | | | |
| Resource AME | 426.5 | 421.6 | 433.5 | 443.4 | 453.2 | 464.7 |
| Resource DEL, excluding depreciation[2] | 330.4 | 360.6 | 384.6 | 400.7 | 417.6 | 435.5 |
| Ring-fenced depreciation | 30.8 | 33.6 | 35.9 | 37.4 | 39.0 | 40.6 |
| Public Sector Current Expenditure | 787.7 | 815.8 | 854.1 | 881.5 | 909.9 | 940.8 |
| CAPITAL EXPENDITURE | | | | | | |
| Capital AME | 33.6 | 30.4 | 26.6 | 26.9 | 28.5 | 29.2 |
| Capital DEL | 65.5 | 81.6 | 96.7 | 102.3 | 106.5 | 110.2 |
| Public Sector Gross Investment | 99.1 | 111.9 | 123.3 | 129.2 | 135.0 | 139.4 |
| TOTAL MANAGED EXPENDITURE | 886.8 | 927.7 | 977.4 | 1010.7 | 1044.9 | 1080.2 |
| Total Managed Expenditure (% GDP) | 39.8% | 40.3% | 40.8% | 40.8% | 40.8% | 40.7% |

*[1] Budgeting totals are shown including the Office for Budget Responsibility (OBR) forecast Allowance for Shortfall. Resource DEL excluding ring-fenced depreciation is the Treasury's primary control within resource budgets and is the basis on which departmental Spending Review settlements are agreed. The OBR publishes Public Sector Current Expenditure (PSCE) in DEL and AME, and PSGI in DEL and AME. A reconciliation is published by the OBR.*

*[2] From 2019-20 Transport DEL includes funding for expenditure by Network Rail. This was formerly part of Department for Transport's Annually Managed Expenditure (AME) budget.*

*Source: Spring Budget 2020*

## Departmental Expenditure Limits

Tables 3.B and 3.C show the departmental resource and capital totals set at Spending Review 2015, Spending Round 2019 and adjusted to reflect subsequent announcements up to Budget 2020. The Budget also sets out the path of day-to-day spending by departments in aggregate for years beyond the current Spending Review period. From 2019-20 to 2024-25, RDEL spending will grow at an average of 3.3% per year in real terms.[1]

From 2019-20 to 2024-25, capital spending will grow at an average of 7.1% a year in real terms. Ahead of the Spending Review, the government has rebased the path of capital spending to reflect the latest expected spending plans over the period to 2024-25. As a result of decisions taken by this Chancellor, in this Parliament, public sector net investment (PSNI) will be triple the average investment over the last 40 years.

## Devolved administrations

The application of the Barnett formula to spending decisions taken by the UK government at the Budget will provide each of the devolved administrations with additional funding to be allocated according to their own priorities. The Scottish and Welsh governments' block grants will be further adjusted as set out in their respective fiscal frameworks.

Other information relevant to the quality of public finances is presented in Chapter 2:

- paragraphs 1.26 to 1.62 deal with the government's fiscal plan.
- paragraphs 3.6 to 3.75 deal with taxes for individuals and business.
- paragraphs 3.76 to 3.91 cover ensuring a fair contribution through the tax system

### Departmental Resource Budgets (Resource DEL excluding depreciation)

| | Plans | |
|---|---|---|
| | 2019-20 | 2020-21 |
| Resource DEL excluding depreciation[1] | | |
| Defence | 133.3 | 139.8 |
| Single Intelligence Account[2] | 123.7 | 129.9 |
| Home Office | 63.8 | 67.8 |
| Foreign and Commonwealth Office[3] | 44.4 | 47.6 |
| International Development[3,4] | 11.5 | 13.0 |
| Health (inc. NHS) | 7.8 | 8.3 |

[1] Growth rate adjusted for technical factors in 2019-20 to ensure consistency between years.

| | | |
|---|---|---|
| of which: NHS England | 0.6 | 0.7 |
| Work and Pensions | 29.5 | 30.8 |
| Education | 2.4 | 2.1 |
| Business, Energy and Industrial Strategy | 2.4 | 1.1 |
| Transport[5] | 8.0 | 9.6 |
| Exiting the European Union | 2.6 | 1.7 |
| Digital, Culture, Media and Sport | 5.2 | 8.2 |
| DCLG Communities | 3.8 | 4.2 |
| DCLG Local Government | 2.5 | 2.5 |
| Scotland[6] | 1.6 | 1.7 |
| Wales[7] | 2.1 | 3.9 |
| Northern Ireland | 0.5 | 0.5 |
| Justice | 5.7 | 5.8 |
| Law Officers Departments | 4.0 | 3.9 |
| Environment, Food and Rural Affairs | 0.4 | 0.2 |
| HM Revenue and Customs | 1.0 | 0.5 |
| HM Treasury | 16.9 | 21.1 |
| Cabinet Office | 12.1 | 12.8 |
| International Trade | 11.2 | 11.5 |
| Small and Independent Bodies | 1.5 | 2.2 |
| Reserves[8] | 0.0 | 6.7 |
| Adjustment for Budget Exchange[9] | 0.0 | -0.1 |
| Total Resource DEL excluding depreciation | 330.4 | 360.6 |
| OBR allowance for shortfall[10] | -0.5 | -3.2 |
| OBR resource DEL excluding depreciation forecast | 329.9 | 357.3 |

1 *Resource DEL excluding depreciation is the Treasury's primary control total within resource budgets and the basis on which Spending Review settlements were made.*

2 The SIA budget in 2017-18 includes transfers from other government departments, which have yet to be reflected in lateryears.

3 Figures for 2018-19 and beyond do not reflect all transfers which will be made from DFID to other government departments, as the cross-government funds have not been allocated for these years.

4 Figures reflect Budget 2018 adjustments made as a result of revised GNI forecasts, as well as previous adjustments made at Autumn Budget 2017 and Autumn Statement 2016.

5 From 2019-20 Transport DEL includes funding for expenditure by Network Rail. This was formerly part of Department for Transport's Annually Managed Expenditure (AME) budget.

6 The Scottish Government's resource DEL block grant has been adjusted from 2016-17 onwards as agreed in the Sottish Government's Fiscal Framework. In 2016-17 an adjustment of £5.5billion reflected the devolution of Stamp Duty Land Tax and Landfill Tax and the creation of the Scottish Rate of Income Tax. In 2017-18 an adjustment of £12.5billion reflects the devolution of further income tax powers and revenues from Scottish courts. In 2018-19 and 2019-20, adjustments of £13.1billionand £13.4billionn also include the devolution of Air Passenger Duty. However, the UK and Scottish Governments have now agreed to delay the devolution of Air Passenger Duty. As a result, the Scottish Government's block grant for 2018-19 and 2019-20 will be re-calculated.

[7] The Welsh Government's resource DEL block grant has been adjusted from 2018-19 onwards as agreed in the Welsh Government's Fiscal Framework. In 2018-19 an adjustment of £0.3 billion reflects the devolution of Stamp Duty Land Tax and Landfill Tax and in 2019-20 an adjustment of £2.3 billion reflects the devolution of the Welsh Rate of Income Tax.

[8] The reserve in 2017-18 reflects allocations made at Main Estimates and Autumn Budget 2017.

[9] Departmental budgets in 2017-18 include amounts carried forward from 2016-17 through Budget Exchange, which has been voted at Main Estimates. These increases will be offset at Supplementary Estimates, so are excluded from spending totals.

[10] The OBR's forecast of underspends in resource DEL budgets.

*Source: Autumn Budget 2018*

## Departmental Capital Budgets (Capital DEL, £ billion)

| | Plans | |
|---|---|---|
| | 2018-19 | 2019-20 |
| Capital DEL | | |
| Health and Social Care | 7.1 | 8.2 |
| Education | 4.6 | 4.5 |
| Home Office | 0.7 | 0.8 |
| Justice | 0.5 | 0.7 |
| Law Officers' Departments | 0.0 | 0.0 |
| Defence | 10.5 | 10.6 |
| Single Intelligence Account | 0.6 | 0.8 |
| Foreign and Commonwealth Office | 0.1 | 0.1 |
| International Development [1] | 2.0 | 4.8 |
| MHCLG Housing and Communities[2] | 8.4 | 13.1 |
| MHCLG Local Government | 0.0 | 0.0 |
| Transport[3] | 14.6 | 17.6 |
| Business, Energy and Industrial Strategy[4] | 11.2 | 12.3 |
| Digital, Culture, Media and Sport | 0.6 | 0.6 |
| Environment, Food and Rural Affairs | 0.8 | 0.9 |
| International Trade | 0.0 | 0.0 |
| Work and Pensions | 0.1 | 0.2 |
| HM Revenue and Customs | 0.3 | 0.4 |
| HM Treasury | 0.1 | 0.0 |
| Cabinet Office | 0.1 | 0.1 |
| Scotland | 4.4 | 5.5 |
| Wales[5] | 2.3 | 2.4 |
| Northern Ireland[6] | 1.4 | 1.7 |
| Small and Independent Bodies | 0.4 | 0.5 |
| Reserves[7] | 0.0 | 3.4 |

| | | |
|---|---|---|
| Adjustment for Budget Exchange[8] | 0.0 | -0.6 |
| Total Capital DEL | 71.1 | 88.5 |
| Remove CDEL not in Public Sector Gross Investment[9] | -11.2 | -13.3 |
| OBR Allowance for shortfall | 0.0 | -3.9 |
| Public Sector Gross Investment in CDEL | 59.9 | 71.2 |

1 Figures for 2020-21 do not reflect all transfers which will be made from DfID to other government departments.

2 MHCLG CDEL budget in 2020-21 includes technical adjustments along with Budget announcements since Budget 2018.

3 *DfT's CDEL budget in 2020-21 includes a net reduction due to business rates retention pilots.*

4 BEIS and other government departments' CDEL budgets increased in 2020-21 to account for the reclassification of R&D in the National Accounts,

5 This includes the 5% needs-based Barnett formula uplift.

6 This includes the 2.5% VAT abatement.

7 *2020-21 adjusted to account for a change in the accounting treatment of leases. This money will be allocated to departments through the Estimates process.*

8 *Departmental budgets in 2020-21 include amounts carried forward from 19-20 through Budget Exchange, which will be voted at Main Estimates. These increases will be offset at Supplementary Estimates in future years so are excluded from spending totals.*

9 Capital DEL that does not form part of the public sector gross investment, including financial transactions in Capital DEL.

*Source: Spring Budget 2020*

# Chapter 4
# Institutional features of public finances

## The fiscal policy framework

In recent years, many governments internationally have used fiscal targets as a tool to demonstrate political commitment to fiscal policy goals. Increasingly they have established independent fiscal institutions (IFIs) to assess compliance with these targets, and to increase trust in the forecasts and analysis on which such assessments are usually based.

In the case of the UK, the Office for Budget Responsibility (OBR) was established in 2010 to "ensure that policy is made on an unbiased view of future prospects, improving confidence in the fiscal forecasts".[1]

## Office for Budget Responsibility

The government established the OBR on an interim basis on 17 May 2010. Since then the OBR has been placed on a permanent, statutory footing through the Budget Responsibility and National Audit Act 2011 (the Act), which received Royal Assent on 22 March 2011.

The OBR is comprised of the Chair of the OBR and 2 other members of the Budget Responsibility Committee (BRC), and 2 non-executive members. It is supported by a civil service staff.

There are three BRC members: Robert Chote (Chair of the OBR), Prof. Sir Charlie Bean and Andy King were appointed by the Chancellor with the approval of the Treasury Select Committee. Andy King was appointed in September 2018 and Prof. Sir Charlie Bean in September 2016. Robert Chote was re-appointed for a second term of office in September 2015, having first been appointed in October 2010. There are two non-executive members: Sir Christopher Kelly was appointed by the Chancellor in June 2017. Bronwyn Curtis OBE was appointed by the Chancellor in June 2018.

## Remit of the OBR

The government's fiscal policy decisions are based on the independent forecasts of the economy and public finances, prepared by the OBR. Since the general election in May 2010, the OBR has produced all the official forecasts of the economy and public finances, independently of ministers.

The Act sets out the main duty of the OBR; to examine and report on the sustainability of the public finances. This duty feeds directly into the Treasury's fiscal objective to deliver sound and sustainable public finances.

As set out in the Act, the OBR's responsibilities include:

[1] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/210667/press_01_10.pdf

- the production of at least 2 fiscal and economic forecasts each financial year, including independent scrutiny of the impact of policy measures and any resultant impact on the forecasts and the main risks and assumptions
- an assessment of the extent to which the fiscal and debt management objectives have been, and are likely to be, achieved alongside these forecasts
- an assessment of the accuracy of the previous fiscal and economic forecasts
- an analysis of the sustainability of the public finances

## Operating framework

The Charter for Budget Responsibility provides guidance to the OBR in line with, and in support of, the provisions in the Act. This guidance helps to explain the role of the OBR within the fiscal framework and provide greater clarity as to the OBR's duty to independently examine and report on the sustainability of the public finances.

This guidance provides for the OBR to investigate the impact of trends and policies on the public finances from a multitude of angles including through forecasting, long-term projections and balance sheet analysis. The OBR must perform its duty objectively, transparently and impartially and on the basis of government policy. This protects the independence of the OBR and ensures a clear separation between analysis (which is the role of the OBR) and policy making (which is the responsibility of ministers). The OBR has complete discretion in the performance of its duty subject to its statutory obligations.

As set out in the Charter, the OBR has additional responsibilities including:

- the production of a fiscal risks statement setting out the main risks to the public finances, including macroeconomic risks and specific fiscal risks, to be produced at least once every 2 years. This requirement was included in amendments to the Charter in October 2015
- the assessment of spending against the welfare cap and margin at the first Budget or fiscal update of each new Parliament, coinciding with the incoming government's setting of a new cap. In addition, the OBR will monitor welfare spending against the pathway and margin at each Budget and fiscal update before the formal assessment against the cap

To ensure credibility of the fiscal framework and protect the independence of the OBR it is vital for there to be transparency in the responsibilities of the OBR. A Memorandum of Understanding established a transparent framework for cooperation between the OBR and the Treasury, as well as other parts of government that the OBR needs to work closely with to perform its forecasting and analytical duties.

The OBR is accountable to Parliament and the Chancellor for the analysis it produces and the way it uses public funds. A framework document sets out the broad governance and management framework within which the OBR operates.

## The fiscal rules

Spring Budget 2020 was delivered within the government's fiscal rules:

- to have the current budget at least in balance by the third year of the rolling, five-year forecast period
- to ensure that public sector net investment (PSNI) does not exceed 3% of GDP on average over the rolling five-year forecast period
- if the debt interest to revenue ratio is forecast to remain over 6% for a sustained period, the government will take action to ensure the debt-to-GDP ratio is falling

The OBR's Budget forecast confirmed that the government delivered the budget within these fiscal rules.

## Accounting and statistics

The independent Office for National Statistics (ONS) and HM Treasury compile monthly statistics for the public sector and sub-sectors, on both a cash and accrued basis. Reconciliation tables between these are produced. The production is guided by the UK's code of practice which is consistent with the United Nations Fundamental Principles of Official Statistics and the European Statistics Code of Practice.

Information on the UK's contingent liabilities is published for all central government departments. The publication of the audited 'Whole of Government Accounts' (WGA), based on International Financial Reporting Standards, extends the coverage across government, with the latest report covering the year ended 31 March 2017. A summary of publicly available information on contingent liabilities is also published in the OBR's 'Fiscal sustainability report'.

WGA is a full accruals based set of accounts covering the whole public sector and audited by the National Audit Office. WGA is a consolidation of the accounts of over 6,000 organisations across the public sector, including central government departments, local authorities, devolved administrations, the health service, and public corporations.

# Annex A
# OBR analysis

The public version of this Annex of the 2020 Convergence Programme will contain analysis prepared by the Office for Budget Responsibility (OBR).

The first three pieces of analysis included are Chapters 2,3, and 4 of the OBR's March 2020 'Economic and fiscal outlook'. They cover, in turn, the economic outlook, the fiscal outlook, and the performance against the government's fiscal targets. The final part of this annex is the executive summary of the OBR's 2018 'Fiscal sustainability report.

# 2 Economic outlook

## Introduction

2.1 This chapter:

- summarises the main economic developments since our previous forecast in March 2019 (from paragraph 2.2), including our latest estimates of the amount of spare capacity in the economy;
- describes our assumptions and judgements in respect of the UK's exit from the EU (from paragraph 2.13);
- highlights the key conditioning assumptions for the forecast, including fiscal and monetary policy, asset prices and the world economy (from paragraph 2.16);
- sets out our real GDP growth forecasts (from paragraph 2.30), including our judgement regarding the growth in the economy's productive potential that underpins our forecasts for actual GDP growth;
- discusses the outlook for the labour market (from paragraph 2.51) and inflation (from paragraph 2.58); and
- outlines our forecast for nominal GDP, which is the key driver of the outlook for the public finance forecasts (from paragraph 2.66), and compares our central forecast with those of selected external organisations (from paragraph 2.79).

## Developments since our previous forecast

2.2 The Foreword to this document describes the timetable that was followed in producing the forecasts presented here. As usual, we closed our pre-measures economy and fiscal forecasts well ahead of the Budget to provide a stable base against which the Chancellor could assess his policy measures. The pre-measures economy forecast was closed on 18 February and the fiscal forecast on 25 February. And they reflect information gathered from financial market prices over the 10 days to 11 February. After that, the only changes relate to Budget measures and other policy announcements, which in this forecast include the new migration regime and the higher National Living Wage (NLW). Since we closed our pre-measures forecast, news about the spread of coronavirus has prompted unusually large movements in asset prices, while other forecasters have been downgrading their assessments of the economic outlook to take account of the possible adverse consequences. The ultimate spread and economic impact of coronavirus are at this stage highly uncertain,

but they represent a clear downside risk to the forecasts presented below. The consequences are, though, most likely to be concentrated in the near term. We discuss the coronavirus-related risks to our economy and fiscal forecasts in Box 2.3 and in Chapter 3.

## Global developments

2.3 Global growth has eased since our previous forecast. In the second half of 2019, GDP in the euro area grew by 0.4 per cent – 0.5 percentage points less than we expected last March, reflecting a continued slowdown in manufacturing and weaker external demand. US GDP grew by 1.0 per cent in the second half of 2019 – in line with our prediction this time last year. GDP growth in China and India also continued to slow during 2019. Global output rose by 3.6 per cent in 2018 and we now estimate it to have expanded by 2.9 per cent in 2019 – a downward revision of 0.6 percentage points from our previous forecast.

2.4 Increased trade barriers and a rise in uncertainty as a result of the trade tensions between the US and China have led world trade and UK export market growth to be significantly slower than world GDP growth. Uncertainty has caused declines in heavily traded capital goods – as firms postpone investment decisions – and industrial inputs that form a large part of global goods trade. World trade rose by 3.7 per cent in 2018 but we estimate that growth slowed to just 1.1 per cent in 2019, reflecting a broad-based slowing in trade growth in the US, China and other advanced economies. UK export market growth also slowed, from 3.0 per cent in 2018 to an estimated 1.5 per cent in 2019.

2.5 Inflation in the advanced economies has also been lower than we forecast last March. Inflation in the euro area was 1.0 per cent in the fourth quarter of 2019, 0.7 percentage points lower than expected. And in the US, inflation was 2.0 per cent in the fourth quarter of 2019, 0.2 percentage points lower than expected.

## UK GDP

2.6 Since our previous forecast, the Office for National Statistics (ONS) has released its 2019 Blue Book. This is the ONS's annual opportunity to introduce methodological changes to the National Accounts, on top of the normal quarterly incorporation of new information into its estimates of economic activity. This year's revisions were relatively minor, with the profile of output growth since the EU referendum little changed. But there were significant revisions to its composition. We discussed these revisions in our 2019 *Forecast evaluation report (FER)*.[1]

2.7 Initial estimates suggest that output grew by 1.4 per cent in 2019, slightly above our March 2019 forecast. Also, quarterly growth was more volatile than we expected. Output rose by 0.6 per cent in the first quarter but then fell 0.1 per cent in the second. This was in large part down to a precautionary build-up of stocks in the run-up to the UK's planned departure from the EU on 29 March, together with car producers bringing forward summer shutdowns into April. The economy returned to growth in the third quarter with GDP expanding by 0.5 per cent, but temporary factors again contributed, including a bounce back in car

[1] OBR, *Forecast evaluation report*, December 2019.

production. Output then stagnated in the fourth quarter, dragged down by a fall in industrial production as the UK's main export markets slowed and car plants were again shut down as a precaution against Brexit-related disruption to supply chains.

## Inflation and the labour market

2.8 CPI inflation was 1.9 per cent in the first quarter of 2019, in line with our previous forecast. Thereafter inflation was lower than expected and declined steadily in the second half of 2019, partly due to lower-than-expected rents and Ofgem reducing its energy price cap in the final quarter.

2.9 Labour market quantities have been stronger than we expected last March – in terms of both employment and hours worked. With GDP growth only slightly stronger than we expected, productivity growth in 2019 was consequently significantly weaker. Overestimating the contribution of productivity to output growth, while simultaneously underestimating the contribution of total hours worked, has been a persistent feature of our recent forecasts. Average earnings growth was weaker than expected in 2019, based on the National Accounts measure employed in our forecast (computed by dividing wages and salaries by the number of employees). Earnings growth on this measure has, though, been weaker than on the headline average weekly earnings (AWE) measure.

## Our latest estimates of the output gap

2.10 The first step in constructing our forecast is to assess how the current level of activity compares with that consistent with stable inflation in the long term (potential output) – the output gap. Potential output cannot be observed directly, but various techniques can be used to infer it, including survey indicators, statistical filters and production functions. Every method has drawbacks and none avoids the need for judgement. We therefore consider a broad range of evidence anew at each forecast:

- Surveys from the Confederation of British Industry (CBI) and the British Chambers of Commerce (BCC) suggest that businesses experienced elevated recruitment difficulties and were operating near capacity in 2019. Both our 'principal components' and 'aggregate composite' estimates derived from these surveys moved into positive territory in 2017 and have remained so, reflecting in particular the heightened recruitment difficulties. But we place little weight on these measures in our overall assessment, as they tend to be quite volatile and have recently suggested implausibly high degrees of overheating.

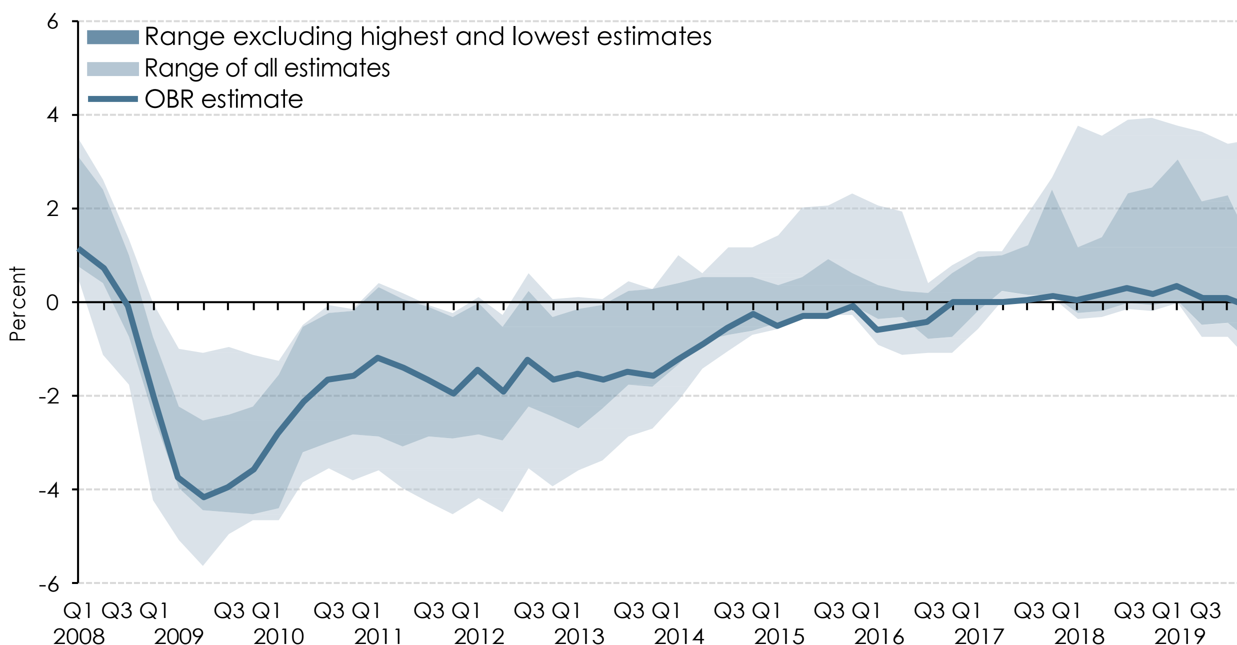
- The two statistical filters that utilise output data alone imply that the economy is currently operating below capacity. We also place limited weight on these measures, as the corresponding estimates of potential output in the recent past are prone to substantial revision as new observations become available, especially when economic conditions change sharply.

- Our other filter-based models augment the output data with ancillary information on the cyclical position. Of these, the 'inflation-augmented' and 'capacity utilisation-augmented' measures point to output lying below potential. We place slightly more weight on these measures at this juncture. The 'unemployment-augmented' measure points to a significant positive output gap.

- Our production function approach, which uses filters to back out the components of potential output, currently points to a negative output gap.[2]

2.11 Chart 2.1 shows the swathe of estimates implied by all our output gap models, as well as a truncated swathe that excludes the highest and lowest estimates. The range of output gap estimates is very wide, reflecting the high degree of uncertainty that surrounds each of the measures. We also sense-check our judgement by comparing the assumed profile for the output gap with the paths for output growth and the unemployment rate. Overall, our current judgement is that the output gap lies in the bottom half of the swathe, and that the economy was operating slightly below potential in the fourth quarter 2019 – by 0.1 per cent, very similar to the margin of spare capacity that we were expecting last March.

## Chart 2.1: Range of output gap estimates




Source: OBR

2.12 Charts 2.2 and 2.3 compare our latest output gap estimates with those of other bodies reported in the Treasury's monthly comparison of independent forecasts. The variation across these estimates is quite low by historical standards. Our estimates lie a little above the average in both 2019 and 2020, but by amounts that are small relative to the uncertainty that lies around any estimate of the output gap.

[2] Our production function approach employs a filter-based estimate of the equilibrium unemployment rate up to 2011, which then falls to our judgement-based central estimate by the second half of 2019.

Chart 2.2: Output gap estimates: 2019

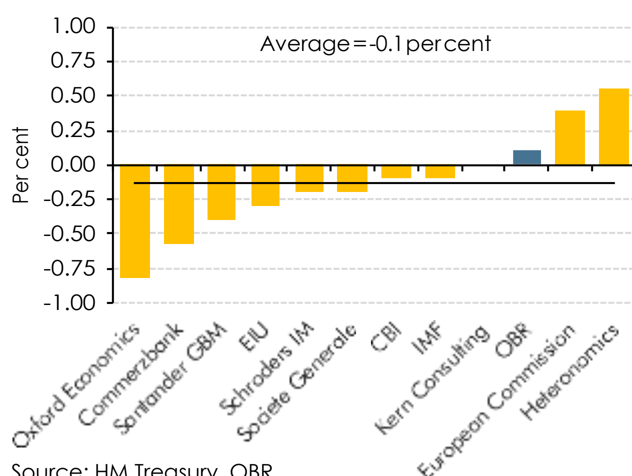
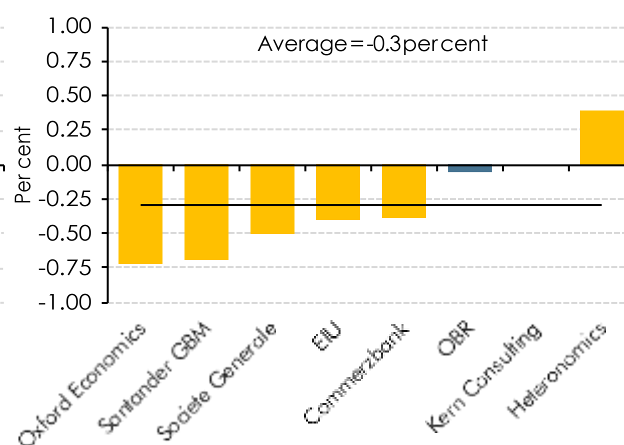



Chart 2.3: Output gap estimates: 2020




Source: HM Treasury, OBR

## Assumptions about the UK's exit from the EU

2.13 The OBR is required by legislation to produce its forecasts based on current government policy (but not necessarily assuming that particular policy objectives will be met). With the nature of the future relationship between the UK and the EU still to be settled, this is not straightforward. We asked the Government if it wished to provide any additional information on post-Brexit policies in relation to trade and migration that would be relevant to our forecasts. As set out in the Foreword, it directed us to its February 2020 paper on the future relationship with the EU and its policy statement on the future migration regime.[3,4] We have incorporated into our forecast an estimate of the effects of introducing the new migration regime from January 2021. As explained in Box 2.4, we have moved from using the ONS 'principal' population projection to the 'zero net EU migration' variant.

2.14 Following the UK's departure from the EU on 31 January, we assume that the current transition period will continue until the end of 2020 – in line with the EU (Withdrawal Agreement) Act. During the transition period, the trading relationship between the UK and the EU is assumed not to change. Thereafter, the UK is assumed to move in an orderly fashion to a new trading arrangement with the EU – although one that must still be painted with a broad brush pending the outcome of negotiations. With our forecast horizon now extending out to the first quarter of 2025, we therefore assume that the UK will be outside the EU single market and customs union for most of the forecast period. Accordingly, we need to take a stance about the likely longer-term impact on UK productivity of greater friction in the trading relationship with the EU. In so doing, we have drawn on the range of external estimates of the effect of a typical free-trade agreement (discussed in Box 2.1). In broad terms, these imply that potential productivity will eventually be around 4 per cent lower than it otherwise would have been, mainly due to extra costs resulting from higher trade barriers and greater impediments to the exploitation of comparative advantage.

[3] HM Government, *The future relationship with the EU: The UK's Approach to Negotiations*, February 2020.
[4] HM Government, *The UK's points-based immigration system: policy statement,* February 2020.

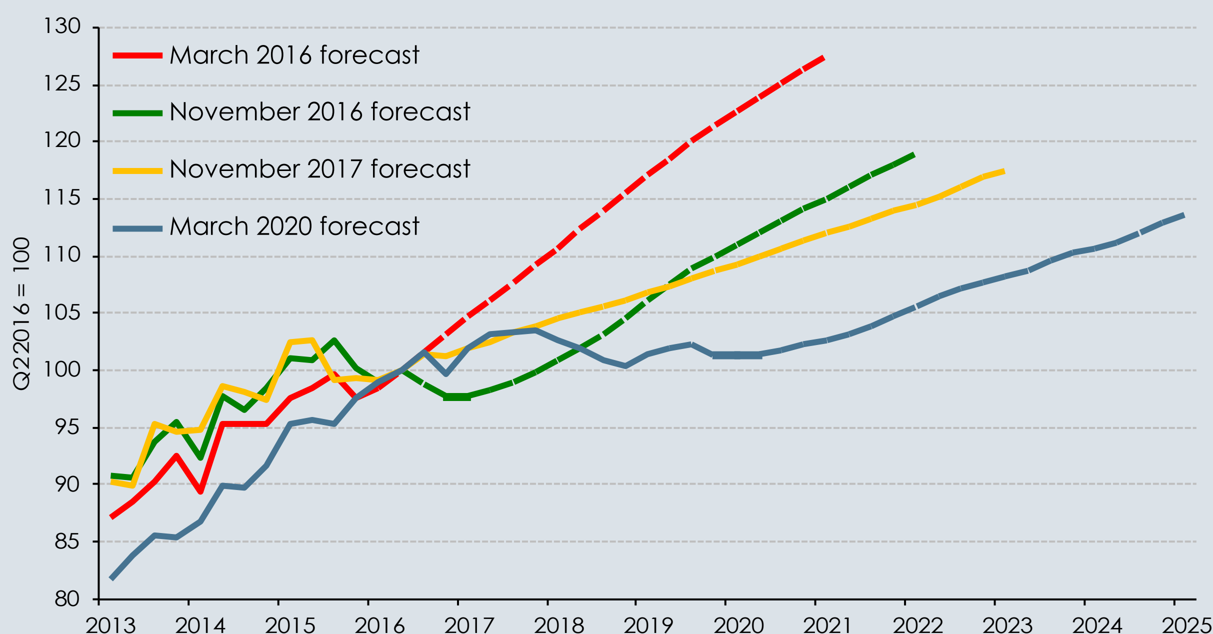
2.15 This assessment does not include any potential offsetting effects from new trade agreements with other jurisdictions or the benefits that might flow if the Government takes advantage of the increased autonomy in its domestic policies; we will consider the effects of these on our future forecasts as and when they are enacted. Our Brexit *Discussion paper* sets out in more detail the channels through which higher barriers to trade with the EU, and any potential offsets, could affect the UK economy and the period over which these might be relevant.[5]

## Box 2.1: The effect on productivity of leaving the EU

In our November 2016 forecast – our first following the EU referendum – we assumed that the UK would leave at the end of March 2019. With the possibility of a transition period, and our forecast extending only to 2021, it was therefore likely that the UK would still be trading under EU rules for most of the forecast period. To form our productivity judgement, we therefore concentrated on the near-term effect of heightened uncertainty on business investment and capital deepening, rather than longer-term effects from higher trade barriers. We anticipated that this would reduce the level of productivity by 1.4 per cent by the first quarter of 2022 – 1.0 percentage points of which was expected to have occurred by now – relative to what would otherwise have happened.

In the event, business investment has been even weaker than we expected immediately after the referendum (Chart A). Recent productivity growth may have also been dampened by a diversion of resources away from productive activities to prepare for Brexit – especially the possibility of 'no deal'.[a] As a result of these two factors, we have increased our estimate of the impact of Brexit on productivity to date, from 1.0 to 1.4 per cent. At least some of these effects may start to unwind once the details of the future trading regime are known.

### Chart A: Successive OBR business investment forecasts




Source: ONS, OBR

[5] OBR, *Discussion paper No. 3: Brexit and the OBR's forecasts*, 2018.

Once the transition period ends, the effect of higher trade barriers on trade intensity and productivity will increasingly come into play.[b] Drawing on available analysis,[c] we have assumed since our November 2016 *EFO* that both exports and imports would be around 15 per cent lower after 10 years than they otherwise would have been. More recent studies confirm that this assumption is broadly consistent with the average estimated effect of leaving the EU, to trade instead under the terms of a typical free trade agreement.[d]

Higher trade barriers impose an additional burden on exporters and importers, lowering (total factor) productivity directly. In addition, they inhibit the exploitation of comparative advantage, leading to lower trade intensity and a less efficient international distribution of production. While some of the adjustment will need to take place quickly, the consequential changes to the UK's industrial structure may be quite drawn out. As a result, the process of adjustment is likely to weigh on productivity growth for several years. Some studies suggest that dynamic effects – for instance through the impact on knowledge transfer – are also possible.[e]

With the outcome of the negotiations still unknown, we have not modelled the long-run impact on productivity and GDP of a specific trading relationship. But, consistent with the formal negotiating objectives of the UK and the EU, we have looked at estimates of the effect of leaving the EU to trade under the terms of a typical free trade agreement. These point to a central estimate of an effect on potential productivity – i.e. including both the effects on total factor productivity and capital deepening – in the region of 4 per cent in the long run (Table A), although the range of estimates is wide.

## Table A: Long-run effect on productivity of trading with EU on FTA terms

| Organisation | Model | Productivity assumption | Per cent<br>Effect |
|---|---|---|---|
| Felbermayr et al (2018) | New quantitative trade model | Constant returns to scale | -1.8 |
| IMF (2018) | Computable general equilibrium | Constant returns to scale | -2 |
| Mayer et al (2018) | New quantitative trade model | Constant returns to scale | -2.4 |
| UK in a Changing Europe (2019) | New quantitative trade model | Constant returns to scale | -2.5 |
| OECD (2016) | NIGEM | Dynamic productivity | -2.7 |
| IMF (2018) | Computable general equilibrium | Melitz-style increasing returns to scale | -3.3 |
| Netherlands CPB (2016) | Computable general equilibrium | Krugman-style increasing returns to scale | -3.4 |
| Bank of England (2019) | Gravity modelling | Dynamic productivity | -3.5 |
| NIESR (2018) | Gravity modelling | Dynamic productivity | -3.8 |
| Whitehall Study (2018) | Computable general equilibrium | Melitz-style increasing returns to scale | -4.9 |
| UK in a Changing Europe (2019) | Gravity modelling | Dynamic productivity | -6.4 |
| Netherlands CPB (2016) | Computable general equilibrium | Dynamic productivity | -5.9 |
| World Bank (2017) | Gravity modelling | Dynamic productivity | -10 |
| Average | | | -4.0 |

With the impact of Brexit on productivity already having reached 1.4 percentage points, according to our estimates, around one third of the long-run impact is, in effect, already in the data. While some of the drag on investment from uncertainty should unwind once uncertainty over the future trading relationship between the EU and UK is resolved, any reversal should be

more than offset by the effect of higher trade barriers on productivity. There is little evidence about the pace at which these effects will be manifest, but we assume that it will take 15 years for the impact to come through in full, but with some front-loading. Specifically, we assume a further third of the long-run productivity effect – in net terms – will take place over our current forecast period and the final third beyond the forecast horizon (and incorporated this effect into our long-term economic determinants, discussed in Annex B). There is, of course, considerable uncertainty about both the size and timing of the effect of Brexit on potential productivity, but it is completely dwarfed by the uncertainty surrounding the underlying path of future productivity growth (also discussed in Annex B).

[a] Bloom *et al*, *The impact of Brexit on UK firms*, August 2019.
[b] OBR, *Discussion paper No. 3: Brexit and the OBR's forecasts*, 2018.
[c] Here we took the average estimated effect from studies by NIESR (*The long-term economic impact of leaving the EU*, National Institute Economic Review no. 236, May 2016), the OECD (*The economic consequences of Brexit: A taxing decision*, OECD policy paper no. 16, April 2016) and LSE/CEP (*The consequences of Brexit for UK trade and living standards*, March 2016).
[d] For example, see: Bank of England, *EU withdrawal scenarios and monetary and financial stability*, November 2018; World Bank, *Deep Integration and UK-EU Trade Relations,* January 2017; NIESR. *The economic effects of the Government's proposed Brexit deal*, November 2018; The UK in a Changing Europe, *The economic impact of Boris Johnson's Brexit proposal*, 2019.
[e] For more details, see OBR, *Discussion paper No. 3: Brexit and the OBR's forecasts*, 2018.

## Other key forecast assumptions and judgements

### Fiscal policy and Budget measures

2.16 Our forecast is conditioned on current government policy and its announced plans for spending and taxes. Relative to our March 2019 forecast, the Government has announced a significant and sustained fiscal loosening. To assess the impact of this on GDP growth we apply a standard set of fiscal multipliers that vary according to the type of tax or spending.[6] Fiscal policy influences the path of real GDP relative to potential in the short to medium term, but we generally assume that it has no lasting effect, as the immediate effects of policy measures fade over time through several mechanisms – for example, the tighter monetary policy needed to keep inflation at target, a stronger exchange rate, and the upward pressure on real wages from a tighter labour market. We explained these assumptions in more detail in our latest *FER*.[7]

2.17 Box 2.2 summarises how our economy forecast has been affected by this fiscal loosening and other small policy changes. Two other policy announcements have had material effects on our medium-term economic forecast: the new migration regime that will be introduced in January 2021 and the further rises in the National Living Wage up to 2024. These are discussed in Boxes 2.4 and 2.5 respectively. Chapter 3 and Annex A describe the corresponding fiscal impacts. Further detail about each Budget measure is set out in the Treasury's documents.

[6] For example, changes in capital spending are assumed to have a multiplier of 1, such that a permanent 1 per cent of GDP increase in capital spending raises GDP by 1 per cent (in the first year).
[7] OBR, *Forecast evaluation report*, December 2019.

## Box 2.2: Economic effects of policy measures

The Government has chosen to loosen fiscal policy materially, with the change dominated by higher departmental spending – both current and capital. To estimate the effect of fiscal policy decisions on GDP growth we use 'multipliers' drawn from the empirical literature.

The bulk of the rise in current spending in 2020-21 on health, education and policing was announced in the 2019 Spending Round. This Budget has increased spending in all future years and by increasing amounts. It has also raised capital spending plans significantly. We expect some of the planned increases to go unspent, as has been the case in the past, particularly when governments try to ramp up capital spending quickly. But even so, our post-measures forecasts for current and capital spending by departments exceed our pre-measures forecasts by 0.5 and 0.6 per cent of GDP respectively by 2024-25. The overall fiscal loosening boosts cumulative real GDP growth by early 2022 by around 0.5 percentage points, with growth slightly weaker than it otherwise would have been thereafter as the effect of the fiscal easing fades.

Over time frames that extend beyond our forecast horizon, higher government investment should boost the supply capacity of the economy. But the extent to which it does so will depend on the mix of projects chosen. Some spending may generate substantial future *social* returns but have little effect on potential GDP – for instance, building more hospitals. Other projects – notably transport infrastructure – are likely to raise potential GDP, but the benefits will probably take a significant amount of time to come through, especially where there are long build times (as with major railway infrastructure). Furthermore, increased competition for scarce construction resources may directly crowd out some private sector investment.

The extra spending on general government investment over the forecast period can be expected eventually to raise the public sector gross capital stock by around 5 per cent. Assuming an output elasticity of 0.1, based on a range of international studies,[a] this suggests an eventual impact on the level of potential productivity of perhaps 0.5 per cent, though that would depend on the precise mix of the extra investment. We have assumed that this would manifest itself largely beyond our forecast horizon. (As we explain in Annex B, if the increase in general government investment as a share of GDP were to be sustained indefinitely, the long-term impact on potential productivity might be of the order of 2.5 per cent.)

We have made several other adjustments to our economic forecast for measures announced in this Budget. The Government has announced several changes that are expected to affect the level of business investment, most importantly a reversal of the planned cut in corporation tax from 19 to 17 per cent, which was due to take effect this April. This more than offsets the expected rise in business investment generated by the more generous structures and buildings allowance and R&D tax credits. When combined, these measures are expected to reduce the level of business investment by 0.3 per cent by the end of the forecast, relative to what we assumed in March 2019.

We have adjusted our inflation forecast to account for the expected impact of freezing all alcohol duties, fuel duty and tuition fees this year, which reduce CPI inflation. Increasing the National Living Wage and reintroducing the tobacco duty escalator that lapsed at the end of the last Parliament more than offsets these. We expect that the combined effect of the policy measures

will add 0.1 per cent to the level of CPI by the end of the forecast period. We have also adjusted the path of inflation to reflect the positive output gap generated by the fiscal easing.

The policy change that has the most significant impact on our house price forecast is the fiscal easing, which boosts real household incomes and house price inflation in the near term. We expect the announced change in the migration regime and the higher Bank Rate profile we have assumed (see paragraph 2.21) to weigh on house price inflation in the medium term.

[a] *Pedro Bom and Jenny Ligthart, "What have we learned from three decades of research on the productivity of public capital?", journal of Economic Surveys (2014).*

## Monetary policy and asset prices

2.18 At its January meeting, the Monetary Policy Committee (MPC) voted 7-2 to hold Bank Rate at 0.75 per cent. It also voted unanimously to maintain the stock of corporate and UK government bond purchases at its current level. This reflected its view that "*the existing stance of monetary policy is appropriate*", following "*early indications of an improved outlook*" based on recent developments in the global economy and falling uncertainty in the UK economy. The MPC has stated that it will closely monitor the extent to which this will be sustained and how it will flow through into domestic activity. The minutes also noted that the "*upcoming Budget may be expansionary*", though by convention the MPC only takes account of government policies that have already been announced in constructing its forecasts.

2.19 We normally derive a future path for Bank Rate from the sterling forward interest rate curve. In this forecast, we adopted that approach in our pre-measures forecast but diverged from it in our post-measures forecast. The path underpinning the pre-measures forecast was based on the average of market prices in the 10 days to 11 February and was consistent with market participants expecting a cut in Bank Rate of around 25 basis points (Chart 2.4). That was, on average, around 0.5 percentage points lower than the corresponding profile at the time of our March 2019 forecast.

2.20 Sterling has been quite volatile over the past 12 months, falling noticeably during the third quarter of 2019, a period of heightened Brexit-related and political uncertainty. It then strengthened towards the end of 2019 after the election, with the sterling effective exchange rate reaching its highest quarterly average since the referendum. We assume that the sterling effective exchange rate will be 2.4 per cent higher than assumed in our March 2019 forecast for the first quarter of 2020. This mainly reflects the strengthening of the pound against the euro more than offsetting the weakening against the dollar over the last year. This represents the starting point for the exchange rate assumption in our pre-measures forecast, which thereafter evolves in line with the spread between domestic and foreign interest rates (Chart 2.5). But, as with Bank Rate, we have diverged from our normal approach in constructing our post-measures forecast.

2.21 In order to produce a coherent economic and fiscal forecast it is important that the assumed paths for Bank Rate and asset prices are, at least broadly, compatible with the main features of our central economic scenario. In particular, the assumed path for Bank Rate needs to be

consistent with inflation meeting the 2 per cent target over the medium term. While our pre-measures forecast shows a small margin of spare capacity over much of the forecast (consistent with a small Bank Rate cut), the substantial fiscal easing in the Budget means that output is projected to be modestly above potential for much of the forecast period in our post-measures forecast (see Chart 2.6). Moreover, the fiscal multipliers that we use to quantify the impact of the fiscal package assume that part of the 'crowding out' of the fiscal impulse is a consequence of the tighter monetary policy stance necessary to keep inflation at target.[8] Taken together, these seem incompatible with the cut in Bank Rate priced into the market curve. Accordingly, we judged it appropriate to adopt a higher path for Bank Rate (and the exchange rate) for the post-measures forecast, consistent with the elimination of the output gap and inflation returning to target within the forecast period.

2.22 The most recent movements in market interest rates have clearly been influenced by expectations about the economic implications of coronavirus, but Bank Rate cuts were priced in even prior to these latest changes. There are several possible explanations:

- Market participants may hold a different view of the appropriate path for Bank Rate than either ourselves or the MPC.[9] That could be because they are more pessimistic about the outlook for demand, more optimistic about the outlook for supply, or believe the natural real rate of interest is lower.

- Market participants hold the same central (median) view as embodied in our forecast but believe the risks are skewed to the downside, so that the mean path that is implied in the market curve lies below the path that would be consistent with the median path. Alternatively, they may believe that the MPC would act more aggressively to the crystallisation of downside risks than it would to upside risks, perhaps because of concerns about the consequences of Bank Rate reaching its effective lower bound.

- Market participants may have underestimated the scale of the Budget package, despite what was signalled in the Conservative Party manifesto, or might have a different view on its implications for the economy and the path of monetary policy. For example, they might have expected the Government to raise capital spending more gradually than has been announced or may implicitly assume smaller fiscal multipliers than ourselves.

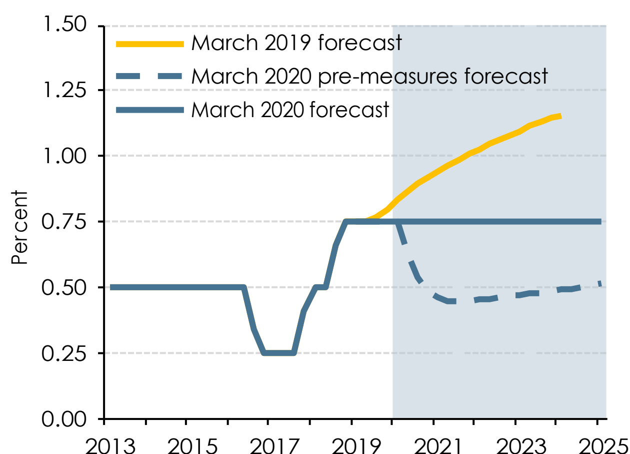
2.23 We are agnostic about the relative importance of these explanations and there is no way of knowing what market participants had priced in with regard to fiscal policy. But for the purpose of calibrating alternative assumptions, we looked at how the paths of Bank Rate and the exchange rate might change if market participants had taken full account of the 2019 Spending Round but not the remainder of the Budget package. We then used a small macroeconomic model[10] to calibrate a suitable joint monetary and exchange rate response sufficient to offset – in the long run – the impact of that 'unanticipated' part of the Budget

[8] See Box 2.2, *Forecast evaluation report*, December 2019.
[9] The MPC's latest central forecast, conditioned on the prevailing market interest rate curve, shows both excess demand and inflation above target at the forecast horizon; see *Monetary Policy Report*, January 2020.
[10] We have used an updated version of the model published in Working Paper No.4 A small model of the UK economy, OBR, July 2012. The model structure is similar though parameter estimates differ due to data updates and re-estimation.

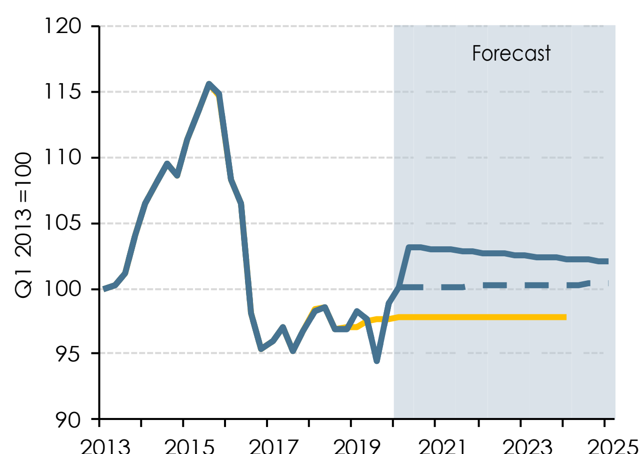
package on output and thus also to meet the inflation target. This suggested a broadly flat path for Bank Rate coupled with an immediate sterling appreciation of around 3 per cent (largely reflecting a modest increase in the underlying equilibrium exchange rate) would suffice – though other combinations are also possible. This analysis forms the basis for the assumptions in our post-measures forecast, with the exchange rate subsequently following a path reflecting the difference between UK and overseas interest rates. On average, our exchange rate assumption is 4.8 per cent above our March 2019 assumption.

2.24 The pre- and post-measures forecasts for Bank Rate and the exchange rate predate the latest market movements triggered by an intensification of coronavirus fears. Several central banks have already cut interest rates in response, including in the US and Australia. The Governor of the Bank of England has said that the shock from coronavirus "*could prove large*" and that policy makers are working on a "*powerful*" response. So the forecasts for interest and exchange rates could well soon be overtaken by events.

## Chart 2.4: Bank Rate




## Chart 2.5: Sterling effective exchange rate




Source: Bank of England, Bloomberg, OBR

2.25 UK equity prices were 2.6 per cent higher in the fourth quarter of 2019 than assumed in our March 2019 forecast. The starting point for the forecast is based on the 10-day average to 11 February, from where we assume they rise in line with nominal GDP. We have not adjusted our equity price forecast for the Budget package, other than via its effects on nominal GDP. Since we closed the forecast, equity prices have fallen sharply, as discussed in Box 2.3; the corresponding fiscal implications are discussed in Chapter 3.

2.26 Sterling oil prices were somewhat volatile during 2019. Oil prices are assumed to fall in the first quarter of 2020 to £45 per barrel, largely due to weakened demand from China after the coronavirus outbreak. We assume oil prices then follow the futures price for the first two years of the forecast and subsequently move in line with major economies' CPI inflation. Sterling oil prices settle at around £41 per barrel over the forecast period, around 12 per cent below our March 2019 assumption. But since we made this assumption, oil prices have been further hit by the escalation of concerns over the effects of coronavirus (Box 2.3).

## World economy

2.27 Our projection for global growth is informed by the forecasts in the IMF's October 2019 *World Economic Outlook* (WEO), its January update and the OECD's November 2019 *Economic Outlook*. In light of these, we revised our forecast down significantly in the near term. We now expect world GDP in 2020 to grow by 3.0 per cent – a downward revision of 0.6 percentage points from our March 2019 forecast (Table 2.1). These revisions are widespread across both the advanced and emerging economies. Some of this revision is due to the outbreak of coronavirus, although the latest estimates suggest that the near-term effect on growth is likely to be significantly greater than we have assumed (Box 2.3). We expect global GDP growth to recover to 3.6 per cent next year.

### Table 2.1: Global GDP and trade growth

| | Percentage change on a year earlier | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
| GDP | | | | | | | |
| Euro area | 1.9 | 1.2 | 1.1 | 1.4 | 1.4 | 1.3 | 1.3 |
| US | 2.9 | 2.3 | 2.0 | 1.7 | 1.6 | 1.6 | 1.6 |
| China | 6.7 | 6.2 | 5.0 | 6.5 | 5.7 | 5.6 | 5.5 |
| World | 3.6 | 2.9 | 3.0 | 3.6 | 3.5 | 3.6 | 3.6 |
| Trade | | | | | | | |
| UK export markets | 3.0 | 1.5 | 1.6 | 3.4 | 3.3 | 3.4 | 3.5 |
| World | 3.7 | 1.1 | 1.9 | 3.9 | 3.6 | 3.7 | 3.8 |

2.28 We expect the slowdown in world trade growth in 2019 to reverse over the following couple of years as trade tensions ease (and given our assumption that the impact of coronavirus would be relatively mild and transient). Even so, we have revised down our forecast for 2020 by 2.0 percentage points and for it to remain well below the growth seen in 2018. We expect world trade growth to pick up further in 2021 and to continue growing robustly thereafter. The near-term downward revisions to world trade growth are much larger than for world GDP, largely reflecting the impact of increased global trade barriers and of coronavirus on globalised supply chains.

2.29 We expect growth in UK export markets to follow a similar profile to that of world trade. We now expect growth of 1.6 per cent in 2020, 1.9 percentage points lower than in our previous forecast, reflecting a continuation of last year's subdued expansion in trade between the advanced economies. Thereafter, growth is expected to pick up noticeably.

## Box 2.3: The potential impact of coronavirus on the economy and public finances

Our global forecast was closed for new data on 14 February. At that point, the coronavirus (Covid-19) outbreak was mostly concentrated in China with only limited spread to other countries. For our central forecast, we assumed that the associated economic disruption would be relatively short-lived and concentrated in China, with some transmission through supply chains to other parts of Asia and Europe. This implied a temporary impact on global GDP and trade, weighing modestly on UK activity in the first part of this year – a mild 'V-shaped' shock.

In calibrating the size of the effect, we were guided by the impact of the 2003 SARS outbreak, which is estimated to have knocked around 1 percentage point off Chinese GDP growth that year.[a] The associated impact on world GDP and trade was, though, quite limited. Since then, the share of China in world GDP and world trade has more than doubled. For that reason, we expected the impact on world GDP and world trade to be somewhat greater.

Bearing this in mind, we lowered our forecast for Chinese GDP growth in 2020 by 1 percentage point (to 5 per cent), with smaller adjustments in other parts of Asia, the US and the euro area, that together reduced world GDP growth by 0.3 percentage points. On this basis we lowered our forecasts for the growth of world trade and UK export markets by 0.5 and 0.2 percentage points respectively. This was expected to knock 0.1 percentage points off UK GDP growth this year.

Since we closed our pre-measures forecast (which serves as a stable basis for the Chancellor's Budget policy decisions), it has become clear that the spread of coronavirus will be far wider than assumed in our central forecast, pointing to a deeper – and possibly more prolonged – slowdown. While the number of confirmed cases in the UK is still relatively small at the time of writing, the Chief Medical Officer, Professor Chris Whitty, has already declared that an epidemic is now "likely" here and the Government has announced plans as to how it would respond.[b]

The intensification of the outbreak overseas will affect the UK through a variety of channels: a more pronounced slowdown in export markets; potential shortages of inputs as supply chains are disrupted; disruption of travel plans and international transport; and the general impact of heightened uncertainty on spending by businesses and households. In addition, a widespread outbreak in the UK would directly impact both supply, as businesses have to operate with a substantially reduced workforce as individuals are placed under quarantine, and demand, as consumers stay at home in order to avoid contact with others.[c]

This is a fast-moving situation and forecasts necessarily become speculative. The OECD's Interim Economic Outlook – released after we closed our forecast – has a 'baseline' scenario that assumes the outbreak is contained and largely centred in China (though much more severe than in our central forecast). In that scenario, world GDP growth slows to 2.4 per cent this year and world trade falls by 0.9 per cent. In its more severe 'domino' scenario, with broad contagion around the globe, the corresponding figures are 1.5 per cent and 3.8 per cent. The implications of slower growth for the public finances, abstracting from any discretionary measures, leads the median advanced economy to experience an increase in the budget deficit of 0.1 per cent of GDP in 2020 in the baseline scenario but more than 0.5 per cent in the more severe one.[d]

At this stage, it is too early to identify any economic impact in ONS data for the UK, but asset prices have moved sharply since we closed the window for financial market data on 11 February

These movements alone would change our fiscal forecast. By the time London markets had closed on 6 March, equity prices had fallen 13 per cent; oil prices by about £7 a barrel; and the market implied path for Bank Rate over the coming years by around 25 basis points (Table B). Plugging these determinants into the main fiscal forecast models that use them would lower receipts in 2022-23 by £3.7 billion (dominated by the effect of lower equity prices on capital gains tax), but also lower spending by £1.5 billion (as the debt interest saving associated with the APF would be greater). So, other things being equal, borrowing would be £2.2 billion higher.

### Table B: Indicative fiscal effects of changes in market determinants

| | Change in determinant | £ billion in 2022-23 | |
|---|---|---|---|
| | | Receipts | Spending |
| Equity prices (per cent)[1] | -13 | -3.2 | |
| Oil prices (£/barrel)[2] | -7 | -0.5 | |
| Market-implied Bank Rate (basis points) | -25 | | -1.5 |
| Total | | -3.7 | -1.5 |

[1] Combined impact on capital gains and inheritance tax.
[2] Combined impact of a fall in North-Sea revenue and a rise in fuel duties.

In the Budget, the Chancellor announced measures intended to mitigate the effects of the more severe potential scenarios. Unavoidably, these were finalised after we closed our economic and fiscal forecasts. It is impossible at this point to give a reliable estimate of their fiscal consequences, as the take-up and implementation will depend on how the outbreak unfolds.

[a] This is consistent with Hai, Zhao, Wang and Hou, *The Short-Term Impact of SARS on the Chinese Economy*, 2004; and Lee and McKibbin, *Estimating the global economic costs of SARS*, 2004.
[b] UK Government, *Coronavirus action plan*, 2020.
[c] For information on how coronavirus may impact the UK we have drawn on CBO, *A potential influenza pandemic: possible macroeconomic effects and policy issues*, 2005; Keogh-Brown, Wren-Lewis, Edmunds, Beutels and Smith, *The possible macroeconomic impact on the UK of an influenza pandemic*, 2009; and McKibbin and Fernando, *The global macroeconomic impacts of COVID-19: Seven Scenarios*, 2020.
[d] OECD, *Interim economic outlook*, March 2020.

## Prospects for real GDP growth

### The path of potential output

2.30 The path for potential output, together with the starting output gap, determine the scope for growth in GDP over the next five years that is consistent with the Bank of England meeting its inflation target over the medium term.

#### Potential hours worked

2.31 There are four elements to our forecast for the potential total number of hours worked: the number of adults in the country; the proportion of them participating in the labour market; the proportion of those that could find employment; and the average number of hours that they would be willing and able to work:

- Population. As a result of the tighter migration regime for EU migrants that is planned for January 2021, we now base our forecast on the ONS 'zero net EU migration' variant, which projects that net inward migration will fall to 129,000 in 2025. This

lowers projected population growth relative to our March 2019 forecast, which reduces potential output (see Box 2.4).

- Participation. We forecast participation rates using the cohort model that underpins our long-term projections.[11] We have revised our assumptions on labour market entry and exit rates to better capture the effect of education policy reforms a decade ago that have affected successive cohorts' labour market activity. This delivers a slightly higher profile for participation than last March, with the rising share of the elderly eventually outweighing increased participation by those on the cusp of retirement.

- Employment rate. Before policy changes, we expected the equilibrium unemployment rate to hold steady at 4.0 per cent. The increase in the National Living Wage is expected gradually to raise this to 4.1 per cent by 2024 (see Box 2.5).

- Average hours. Before policy changes, we expected equilibrium average hours to be broadly flat across the forecast period. The increase in the National Living Wage is expected to lower average hours slightly (also described in Box 2.5).

## Box 2.4: The new immigration system

In February, the Government announced its intention to introduce a 'points-based' migration system from January 2021 that will align migration policy for EU and non-EU migrants. The new regime requires migrants to speak English, have a job offer from an approved sponsor, and meet skills and salary thresholds. Tier 2 General applicants will need to earn the higher of the 25th percentile of their occupation's wage distribution or £25,600 – slightly below the £30,000 specified in the Government's December 2018 White Paper. Potential migrants will also be able to trade a salary lower than the going rate against characteristics such as their qualifications.

Relative to the current regime, this is more restrictive for EU migrants but modestly less so for non-EU migrants. It shares many features with the current system for non-EU migrants, but with a lower salary threshold. Even so, successful implementation of the new regime by the January deadline looks challenging.

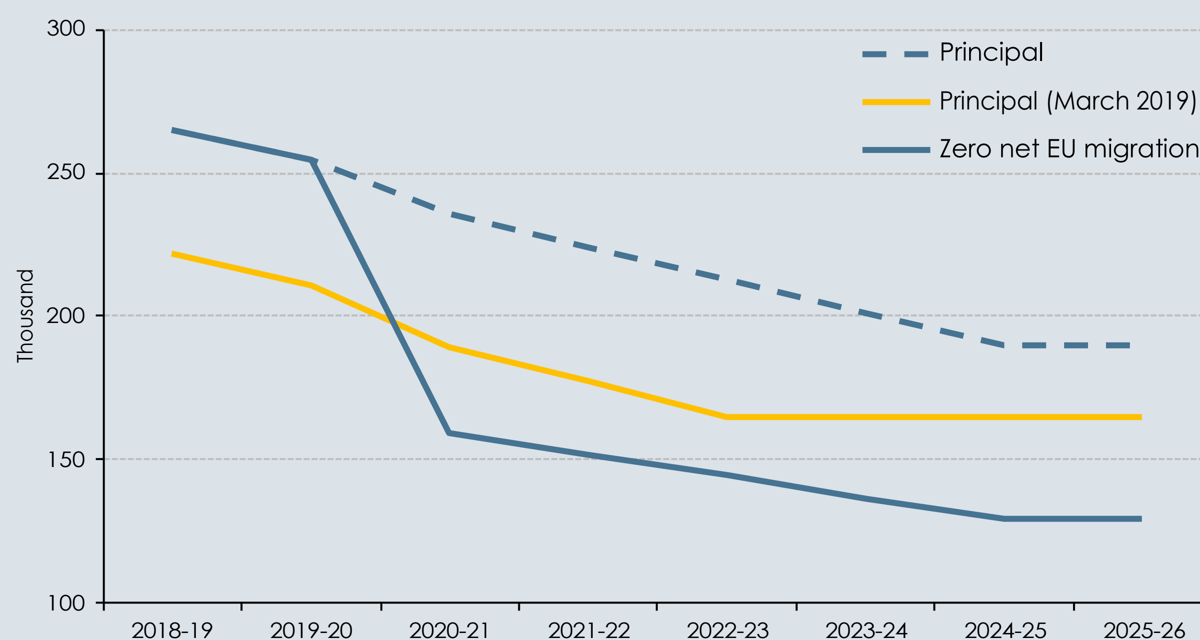
In its latest report,[a] the Migration Advisory Committee modelled the impacts on migration of a counterfactual scenario in which the UK was assumed to have adopted in 2004 the more restrictive regime outlined in the Government's earlier White Paper (which proposed a salary threshold of £30,000). This counterfactual was then compared with actual migration flows to get a sense of the impacts by 2016-18. It concluded that cumulative EEA migration would have been 70 per cent lower, with the overall population 3.2 per cent smaller, employment 4.0 per cent lower, GDP per worker 1.3 per cent higher and therefore overall output 2.8 per cent lower.

Our March 2019 forecast was based on the ONS's 'principal' population projection for net migration to decline to 165,000 a year in 2023. Last October, the ONS revised up the level of net migration in the 'principal' projection to settle at 190,000 in 2025, which we incorporated in our pre-measures forecast. To reflect the more restrictive regime, in our post-measures forecast

[11] Annex A of our July 2014 *Fiscal Sustainability Report* discusses our longer-term approach to labour market modelling in more detail.

we have switched to the 'zero net EU migration' variant, in which net migration flows fall to 129,000. The profile for this variant strikes us as a reasonable depiction of how net inward migration might evolve as a result of introducing the new migration regime, though that does not imply that our central expectation of net EU migration itself is exactly zero. Indeed, we would expect falls in net migration from the EU to be partly offset by increases in net migration from those outside the EU. Recent years suggest an offset of around half might be expected. Uncertainty around migration projections is always large,[b] with the change in migration regime only adding to this uncertainty.

### Chart B: Net inward migration in ONS population projections




Source: ONS

These changes reduce the expected size of the population and, alongside a small fall in the participation rate, reduce total participation by 0.4 per cent at the forecast horizon. We assume no effect on equilibrium unemployment, so the full effect feeds through into lower employment.

The productivity impact is more difficult to judge. The salary threshold imposed on new migrants will, arithmetically, lead to a 'batting average' effect as some low wage – and therefore in most cases also low productivity – workers will no longer be able to enter the country, thereby raising average productivity relative to the current regime. Based on the available evidence, we assume this increases potential output per worker by 0.1 per cent – broadly offsetting the fall in the participation rate and around a quarter of the total employment effect.[c]

[a] Migration Advisory Committee 2020 *A Points-Bases System and Salary Thresholds for Immigration: report.*
[b] We have outlined the challenges in forecasting net migration in *Discussion paper No.3 Brexit and the OBR's forecasts*
[c] Home Office *Technical Paper to accompany 'The UK's future skills-based immigration system economic appraisal: Annex B'* 2018 and HM Government *EU Exit: Long-Term Analysis Technical Reference Paper*, 2018.

## Potential productivity

2.32 The outlook for potential productivity is the most important, yet most uncertain, element of potential output. Several factors are relevant to our overall judgement:

- Productivity growth has been weak globally since around the time of the financial crisis, with the slowdown more pronounced in the UK than in most other countries. We continue to expect some recovery from the recent sustained period of low growth, though we have revised down our long-term assumption (see Annex B).
- The recent extreme weakness of UK productivity growth in part reflects the stagnation of business investment since the EU referendum (see Box 2.1). We expect a gradual pick-up in business investment growth after the end of the transition period, as some of the uncertainty regarding the future economic relationship between the EU and UK is resolved. But it will take time for businesses to adapt to the new regime, so that recovery in investment is initially likely to be muted. In addition, the necessary structural change in the economy following Brexit is likely to prompt firms to scrap some capital earlier than they otherwise would have done.
- Some of the recent weakness in productivity may have reflected a diversion of people away from productive activities to prepare for Brexit – especially the possibility of 'no deal' – so lowering total factor productivity (TFP). Together with the weakness in business investment, we estimate this already to have reduced potential productivity by around 1.4 percentage points. At the end of the transition period, businesses will be faced with the additional costs associated with the new trade barriers, further dampening TFP. Ultimately, we expect productivity to be around 4 per cent lower than it would otherwise have been, though it will take some years for these effects to work through in full (see Box 2.1).
- A tighter labour market may exert pressure on firms to extract more output from their existing workforce. In addition, shifts in the composition of the workforce induced by the new migration regime can be expected to generate a small upward impetus to productivity growth, worth around 0.1 percentage points relative to the current regime by the end of the forecast period, while the planned increase in the NLW is expected to add around 0.2 percentage points.
- The significant planned increase in public investment potentially boosts productivity by raising the public capital stock, but we have assumed that the effect is likely to be felt mainly beyond our forecast horizon (see Box 2.2 and Annex B).

2.33 Our projection for potential productivity is formed as a top-down judgement, but reflects the net effect of these varied and conflicting forces. We continue to assume that potential productivity growth will rise gradually over the forecast period, reaching 1.3 per cent in 2024. The profile is, however, lower than we assumed last March, owing to the recent weakness in outturn data, subdued business investment growth and the incorporation of the effect of higher trade barriers on productivity growth within the forecast horizon.

2.34 In respect of the particular impact of Brexit, an unwinding of the adverse effect of heightened uncertainty on business investment since the referendum should be more than offset by higher trade barriers weighing on TFP. Overall, we estimate that around a third of the final Brexit effect on productivity of around 4 percentage points is, in effect, already in the data; another third will be felt over our forecast period; and that the remaining third will work through gradually beyond our forecast horizon.

### Potential output

2.35 Overall, relative to March 2019, the downward revisions to potential productivity growth, equilibrium average hours, and population growth, along with the upward revision to the equilibrium unemployment rate, outweigh the upward revision to the potential participation rate. As a result, potential output growth averages 1.4 per cent a year between 2019 and 2023, down from 1.6 per cent in March 2019.

### Table 2.2: Contributions to potential output growth

| | Percentage points, unless otherwise stated | | | | | |
|---|---|---|---|---|---|---|
| | Population[1] | Participation and unemployment[1] | Average hours | Productivity[2] | Potential output[3] | *memo: Equilibrium unemployment rate (per cent)* |
| 2019 | 0.5 | 0.1 | 0.0 | 0.9 | 1.4 | 4.0 |
| 2020 | 0.6 | 0.1 | -0.2 | 0.8 | 1.2 | 4.0 |
| 2021 | 0.5 | 0.0 | -0.1 | 1.0 | 1.4 | 4.0 |
| 2022 | 0.5 | -0.1 | 0.0 | 1.1 | 1.4 | 4.1 |
| 2023 | 0.5 | -0.2 | 0.0 | 1.2 | 1.5 | 4.1 |
| 2024 | 0.5 | -0.2 | 0.0 | 1.3 | 1.6 | 4.1 |
| | 2019-2023 average | | | | | |
| March 2019 forecast | 0.5 | -0.1 | 0.0 | 1.1 | 1.6 | 4.0 |
| March 2020 forecast | 0.5 | 0.0 | -0.1 | 1.0 | 1.4 | 4.0 |
| Difference | 0.0 | 0.1 | -0.1 | -0.1 | -0.2 | 0.0 |

[1] Corresponding to those aged 16 and over.
[2] Output per hour.
[3] Components may not sum to total due to rounding.

## Oil and gas output

2.36 Our potential output forecast excludes the small, but volatile, oil and gas sector. So to produce our GDP forecast we need a forecast for oil and gas production. Our production forecasts are informed by the projections published by the Oil and Gas Authority (OGA). Based on the OGA's latest *Stewardship Survey*, we have revised production up compared to March 2019. That largely reflects higher-than-expected production in 2019, which we assume will persist over the forecast. Our oil and gas expenditure forecasts are also informed by OGA projections. We have revised overall expenditure down since last March, reflecting weaker spending both in 2018 and 2019.

## The short-term outlook for GDP

2.37 Following the weak end to 2019, we expect a return to growth in the first quarter of 2020. Although few hard data are currently available – the first estimate of January GDP was not available until 11 March – surveys suggest a pick-up in activity in the first two months of the year. In January, the IHS Markit/CIPS Purchasing Managers Index (PMI) rose to its highest level since September 2018 (albeit still below the historical average) and there was a similar improvement in CBI's growth indicator, while Deloitte's CFO Survey and the Bank of England's Decision Maker Panel both pointed to improved business sentiment. The PMI edged up slightly in February, however there was some suggestion that the rebound in activity was losing momentum due to coronavirus-related disruptions.

2.38 Taking all this into account, we expect quarterly GDP growth to be 0.2 per cent in the first quarter of 2020, including some small and temporary downward effect from the disruption caused by coronavirus. We expect quarterly growth to strengthen through the rest of the year, as the initial effects of the fiscal loosening begin to build and our expectation – at the time we finalised the forecast – that the coronavirus effect unwinds. For 2020 as a whole, we forecast GDP growth of 1.1 per cent, 0.4 percentage points below our estimate last March. This reflects the deterioration in the global outlook and the slowdown in UK growth at the end of 2019, which was likely partly due to ongoing Brexit-related uncertainty.

### Table 2.3: The quarterly GDP profile

| | Percentage change on previous quarter | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2019 | | | | 2020 | | | | 2021 | | | |
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| March 2019 forecast[1] | 0.2 | 0.3 | 0.3 | 0.3 | 0.3 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 | 0.4 |
| March 2020 forecast[2] | 0.6 | -0.1 | 0.5 | 0.0 | 0.2 | 0.4 | 0.5 | 0.5 | 0.5 | 0.4 | 0.4 | 0.4 |
| Change[3] | 0.4 | -0.4 | 0.2 | -0.3 | -0.1 | 0.0 | 0.1 | 0.1 | 0.1 | 0.0 | 0.0 | 0.0 |

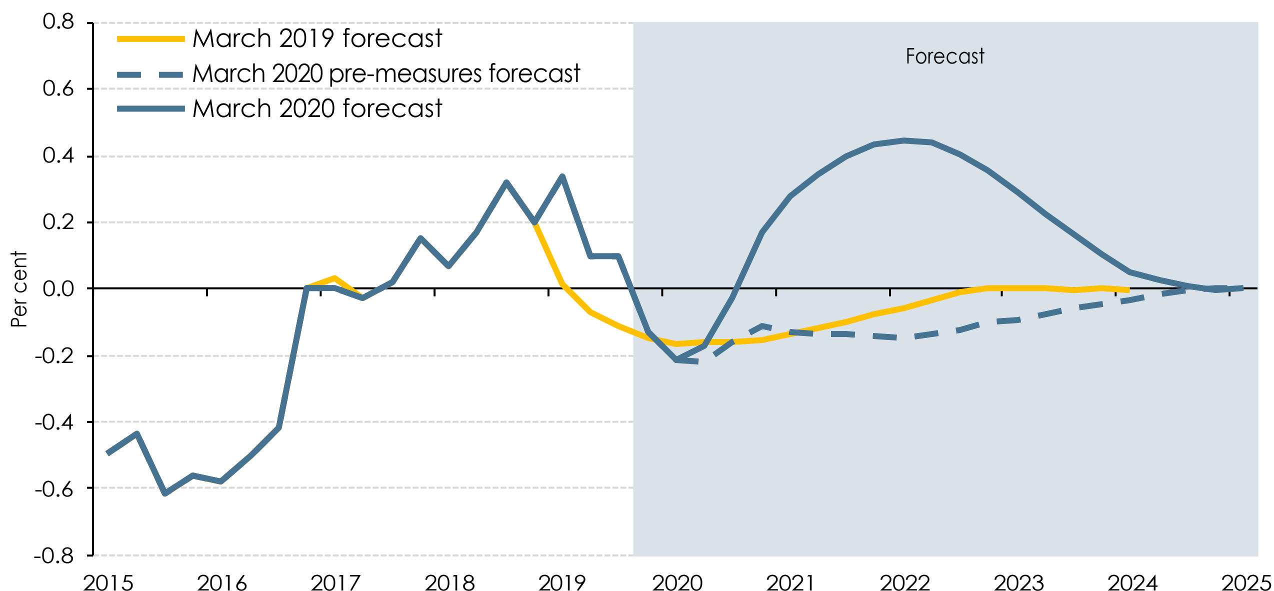
[1] Forecast from the first quarter of 2019.
[2] Forecast from the first quarter of 2020.
[3] Changes may not sum due to rounding.

## The medium-term outlook for GDP

2.39 The peak impact of the fiscal easing on GDP occurs in 2021. Along with the lifting of uncertainty, as the UK moves smoothly (we assume) to a new trading relationship with the EU, this raises GDP growth to 1.8 per cent in 2021, pushing output above potential as shown in Chart 2.6. As the effect of the fiscal expansion dissipates and the tighter migration regime and labour market implications of a higher NLW continue to build, we expect GDP growth to ease to an average of a little under 1½ per cent for the rest of the forecast period, as the output gap gradually closes.

2.40 Before incorporating the fiscal stimulus, we had forecast output to fall further below potential in 2020, reflecting the subdued growth in the UK's export markets and the continuing impact of uncertainty regarding the consequences of Brexit. We then expected growth to pick up, closing the output gap by the end of the forecast period.

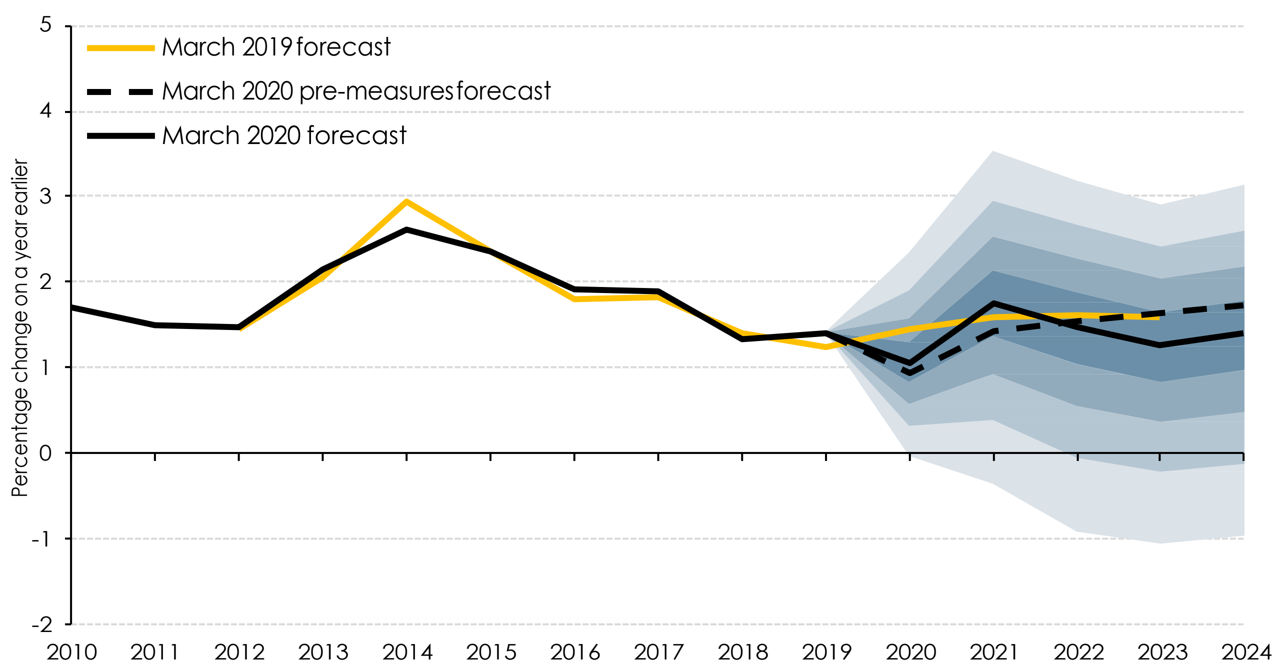
## Chart 2.6: Output gap




Note: Output gap estimates on a quarterly basis, based on the latest National Accounts data and expressed as actual output less potential output as a percentage of potential output (non-oil basis).
Source: OBR

2.41 There is of course significant uncertainty around our central projection for GDP growth. Chart 2.7 shows the likelihood of different outcomes surrounding the central forecast based on the historical distribution of official forecast errors. The solid black line shows our median forecast, with successive pairs of lighter shaded areas around it representing 20 per cent probability bands. The chart implies a roughly 10 per cent probability that GDP will fall in 2020, and the same probability that growth will exceed 2.5 per cent. But it should be emphasized that past forecast errors may not be a guide to future economic shocks.

## Chart 2.7: Real GDP growth fan chart



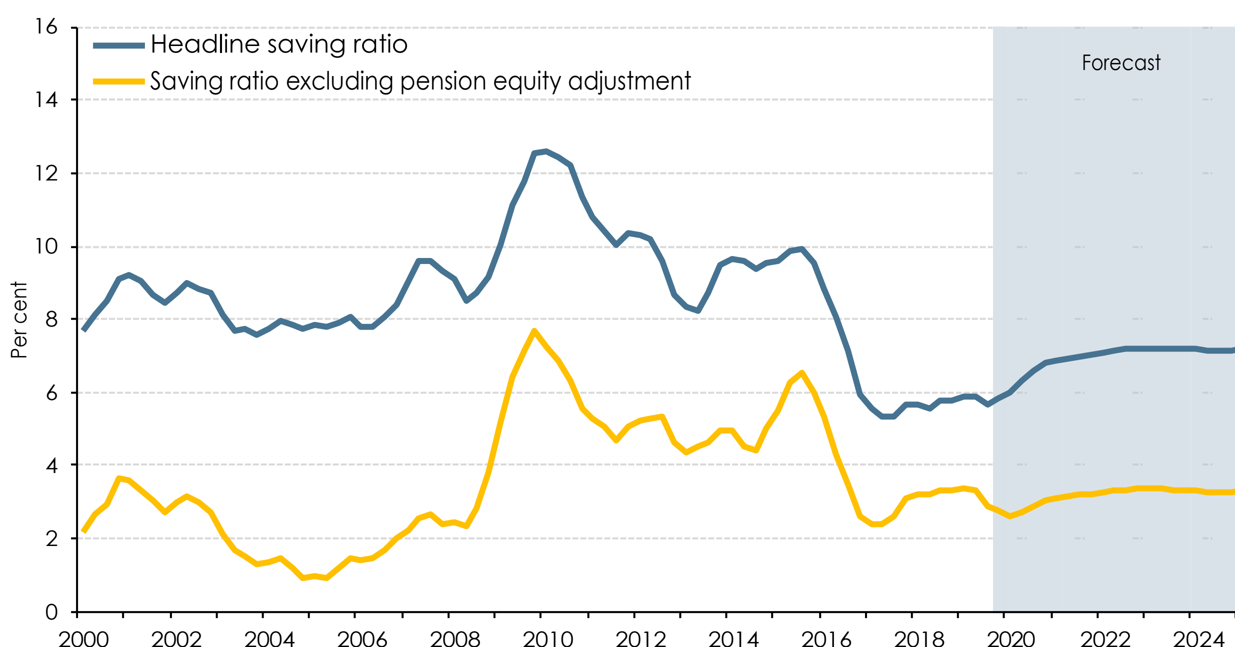

Source: ONS, OBR

# Expenditure composition

## Domestic demand

2.42 We expect private consumption to be relatively subdued in 2020, rising by 1.1 per cent, broadly in line with real household incomes. Real consumption growth is expected to be slightly below real income growth over the forecast. The fiscal expansion, which pushes output above potential, also induces tighter financial conditions that crowd out some private consumption. As a result, the household saving ratio rises from 6.6 per cent in 2020 to 7.2 per cent by the end of the forecast (Chart 2.8), closer to its pre-crisis average.

### Chart 2.8: The household saving ratio




Source: OBR

2.43 Our forecast for government consumption is driven by the new spending plans set out in the Budget. Real government consumption rises by 3.7 per cent in 2020 – the largest annual increase since 2005 – and then at an average of 2.3 per cent a year for the rest of the forecast period, up from 1.6 per cent in our March 2019 forecast. In nominal terms, government consumption ends the forecast at 20.2 per cent of GDP. Back in December 2014, when the Coalition Government pencilled in continuing cuts in medium-term departmental spending totals, government consumption had been projected to fall to a post-war low of 14.7 per cent of GDP at the forecast horizon.

2.44 We expect the weakness in business investment in 2019 to continue into 2020 – it rose by just 0.3 per cent in 2019 and we expect it to be flat in 2020 – due to the lingering impact of Brexit uncertainty. We then expect a modest recovery in 2021 with investment growing by 1.8 per cent, as waning uncertainty regarding the new trading relationship with the EU leads to the implementation of some deferred investment. Relative to our March 2019 forecast, business investment growth is weaker due to the reversal of the planned cut in the corporation tax rate and some crowding out caused by the fiscal expansion.

2.45 Real residential investment contracted by 0.3 per cent in 2019 and we expect this weakness to intensify this year, with residential investment falling by around 4 per cent, reflecting the recent fall in housing starts and subdued turnover in the housing market. Growth is expected to pick up later in the forecast period – reaching around 1.5 per cent – as turnover in the housing market picks up and as real earnings growth rises. The relatively weak profile partly reflects the large increase in public investment, which increases competition for resources and raises costs in the construction sector, reducing activity.

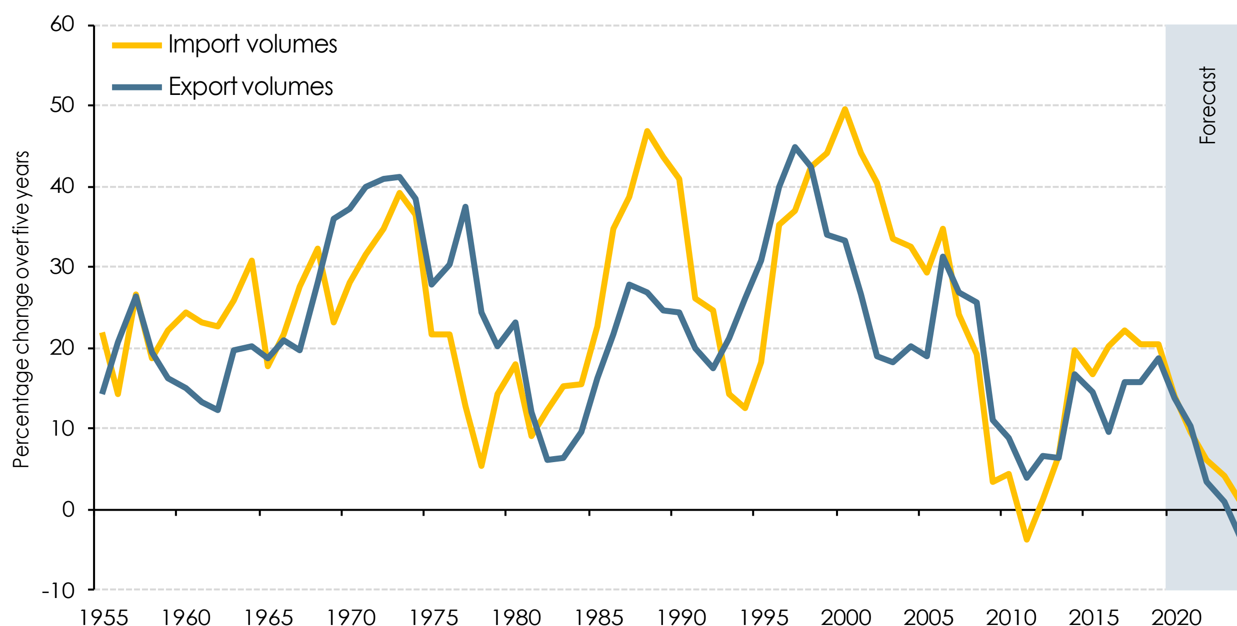
2.46 In contrast to the relatively subdued outlook for private investment, government investment is expected to increase significantly over the forecast period thanks to the Budget spending decisions. We now expect real government investment to increase by around 11 per cent in 2021, up from 2.2 per cent in March 2019. Although year-on-year changes in public investment can be volatile, this would be the largest increase since 2008, when existing capital spending plans were brought forward to provide a fiscal stimulus in response to the financial crisis. General government investment growth averages 4.8 per cent a year from 2020 and 2023, up from 1.8 per cent in March 2019.

### Trade

2.47 Brexit-related stockpiling ahead of both the March and October deadlines meant that both import and export growth were stronger in 2019 than we forecast last March. Imports rose as UK firms built up inventories of goods manufactured in the EU, while exports rose as their EU counterparts did the same. We expect this strength to unwind in 2020, with exports falling by 0.6 per cent and imports by 0.2 per cent. Given the significantly weaker outlook for world trade compared to last March, along with the frictions introduced by the new trading relationship with the EU in 2021, we expect exports to fall modestly throughout the forecast. This weakness is exacerbated by the appreciation of the exchange rate, which we have assumed will accompany the fiscal easing. Between 2019 and 2024 we expect exports to contract by a total of 3.6 per cent.

2.48 Due to a slowdown in import growth towards the end of 2019, and weaker domestic demand, our forecast for import growth in 2020 is significantly lower than last March. Over the rest of the forecast, however, we expect imports to be marginally stronger than in March partly due to a stronger pound boosting import volumes. Given the relative strength of imports compared to exports, the outlook for net trade has deteriorated since March. We now forecast that net trade will subtract from GDP growth every year and by a cumulative 1.7 percentage points between the second quarter of 2020 and the first quarter of 2025 (we expect the first quarter of 2020 to be distorted by trade in non-monetary gold).

## Chart 2.9: Trade growth




Source: Bank of England, OBR

2.49 The relative contributions of the components of demand to GDP growth are summarised in Table 2.4. Growth in government expenditure is forecast to contribute over half of combined GDP growth this year and next, despite accounting for only around a fifth of GDP. In the near term, valuables and inventories also have an impact. The former due to the large movements in non-monetary gold in 2019, while the latter is driven by the accumulation of stocks in the run-up to the two Brexit deadlines in 2019.

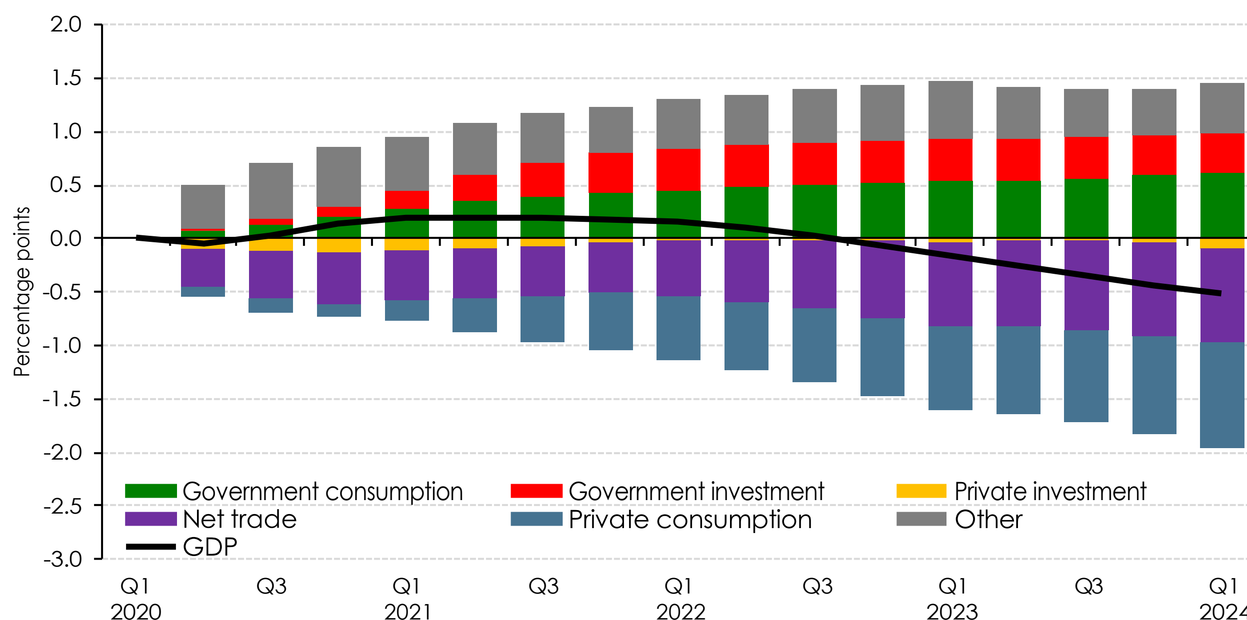
## Table 2.4: Expenditure contributions to real GDP

| | Percentage points, unless otherwise stated | | | | | |
|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | |
| | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
| GDP growth (per cent) | 1.4 | 1.1 | 1.8 | 1.5 | 1.3 | 1.4 |
| *Main contributions:* | | | | | | |
| Private consumption | 0.8 | 0.7 | 0.8 | 0.8 | 0.9 | 0.9 |
| Business investment | 0.0 | 0.0 | 0.2 | 0.3 | 0.2 | 0.2 |
| Dwellings investment[1] | 0.0 | -0.2 | 0.1 | 0.1 | 0.1 | 0.1 |
| Government[2] | 0.7 | 0.8 | 0.8 | 0.6 | 0.4 | 0.5 |
| Change in inventories | 0.1 | -0.1 | 0.1 | 0.0 | 0.0 | 0.0 |
| Net trade | 0.0 | -0.1 | -0.3 | -0.2 | -0.4 | -0.3 |
| Other[3] | -0.2 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |

[1] The sum of public corporations and private sector investment in new dwellings, improvements to dwellings and transfer costs.
[2] The sum of government consumption and general government investment.
[3] Includes the statistical discrepancy and net acquisition of valuables.
Note: Components may not sum to total due to rounding.

2.50 Chart 2.10 shows the revision to our real GDP forecast relative to March 2019 broken down by expenditure component, with a stronger contribution from government and a weaker one from the private sector, mainly because we expect the fiscal easing to crowd out net trade, private consumption and private investment.

Chart 2.10: Expenditure contributions to the cumulative change in real GDP growth




Note: The comparison begins in Q2 2020 as contributions in Q1 2020 are distorted by trade in non-monetary gold.
Source: OBR

## Labour market

### Participation, employment and productivity

2.51 The participation rate increased slightly in the fourth quarter of 2019, to a little above our estimate of its underlying equilibrium rate. We expect participation to fall to its equilibrium rate in the near term, and stay in line with it as the rate declines over the forecast thanks to population ageing. As explained in paragraph 2.31, we have revised up our forecast for the equilibrium participation rate over the forecast period since March 2019.

2.52 The unemployment rate fell to 3.8 per cent in the fourth quarter of 2019, slightly below our estimate of its equilibrium rate of 4.0 per cent. We expect the unemployment rate to fall slightly in the near term thanks to the fiscal easing, and then edge up as growth falls back. The unemployment rate rises slightly over the forecast period as a whole due to the modest effect of the increase in the NLW (Box 2.5) on the underlying equilibrium rate.

2.53 Employment growth across the forecast is somewhat weaker than in our March 2019 forecast, with the downward revision in population growth, and upward revision in the equilibrium unemployment rate, offsetting the effect of the upward revision to the participation rate. Whole economy employment increases by around 520,000 over the forecast period, but the large increases in government spending mean that we expect an

increase in government employment to account for virtually all (490,000) of the rise.[12] This would reverse all the post-2010 fall in government employment. In our pre-measures forecast, the figures for whole economy and general government employment would have been 720,000 and 350,000 respectively, with lower migration the largest factor reducing total employment growth and higher public spending raising the share of it accounted for by government employment.

2.54 Having moved to a lower migration variant, net inward migration now accounts for around 45 per cent of population growth over the forecast period. In our pre-measures forecast, this would have been over 50 per cent. Absent net migration, employment would have fallen slightly in our post measures forecast as the age structure of the native population means that a fall in the participation rate would offset a rise in population.

2.55 Productivity growth has remained stubbornly weak. Some of this weakness looks temporary, for example, because some business investment has been postponed until more clarity about the future trading relationship between the UK and the EU emerges. When combined with the downward revision to our forecast for potential productivity growth, that means that we expect cumulative growth in actual productivity between the fourth quarter of 2019 and first quarter of 2024 of 4.8 per cent – down from 5.2 per cent in March 2019.

## Earnings

2.56 We use an implied measure of average earnings constructed by dividing the National Accounts measure of wages and salaries by the number of employees, rather than the official ONS average weekly earnings (AWE) series. This allows us to fit our earnings forecast directly into the National Accounts framework on which our economy forecast is based – particularly the measure of wages and salaries that is an important determinant of tax receipts. The two series have diverged in the past few quarters, but given the more consistent messages coming from the AWE and HMRC's real-time information (RTI), we have chosen to put more weight on these in informing our forecast judgements.

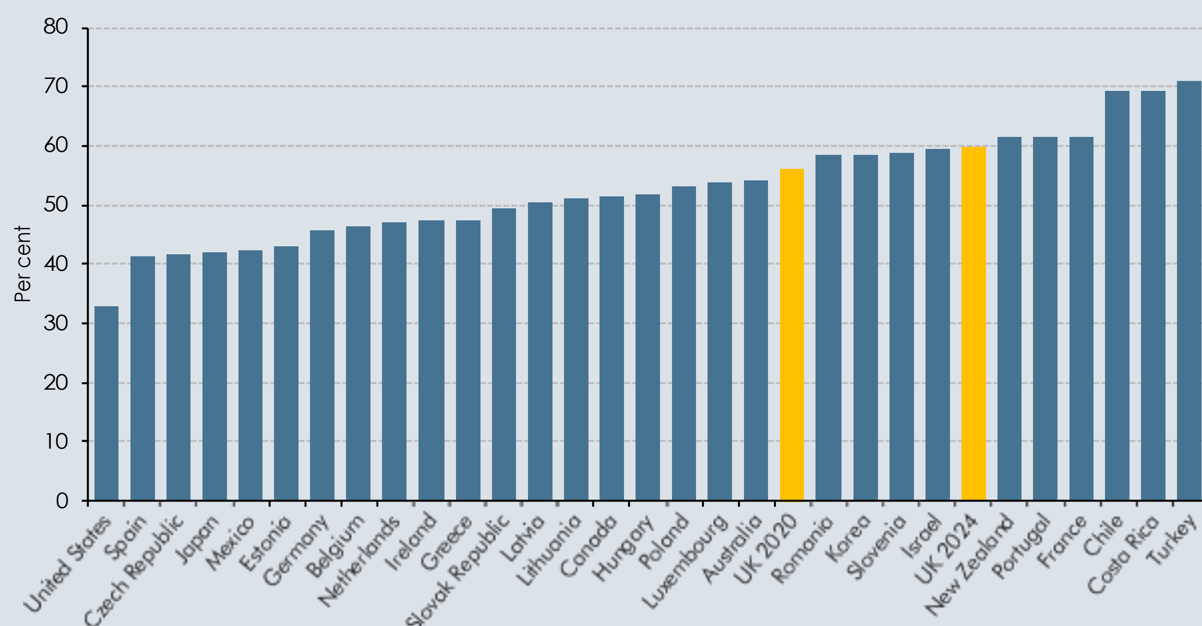
2.57 We estimate that the National Accounts measure of average earnings grew by 2.8 per cent in 2019. This outstripped the sum of productivity growth and whole-economy inflation, resulting in a higher labour share of income. In the near term, we expect earnings growth to pick up alongside a rise in productivity growth – peaking at 3.6 per cent in 2021. Following this, we expect earnings growth to drop back to around 3 per cent, as productivity growth slows and firms partially rebuild their margins which have been squeezed recently.

[12] We use a top down approach for general government employment growth, combining estimates of pay bill growth and the growth of pay bill per head to generate a forecast for employment growth. More information about this approach can be found in the November *2010 Economic and Fiscal Outlook.*

## Box: 2.5: The National Living Wage

The Government has introduced a new target for the National Living Wage (NLW) to reach two-thirds of median earnings (of the relevant population) by 2024, providing economic conditions allow. The age threshold will also be reduced from 25 to 21, starting with a move to age 23 from 2021. This will raise the NLW to a level above that in most other countries (Chart C), so there are relatively few international precedents to draw on to estimate the potential effects. This increases uncertainty around the potential impact.

### Chart C: Adult minimum wage relative to full-time median earnings in 2018



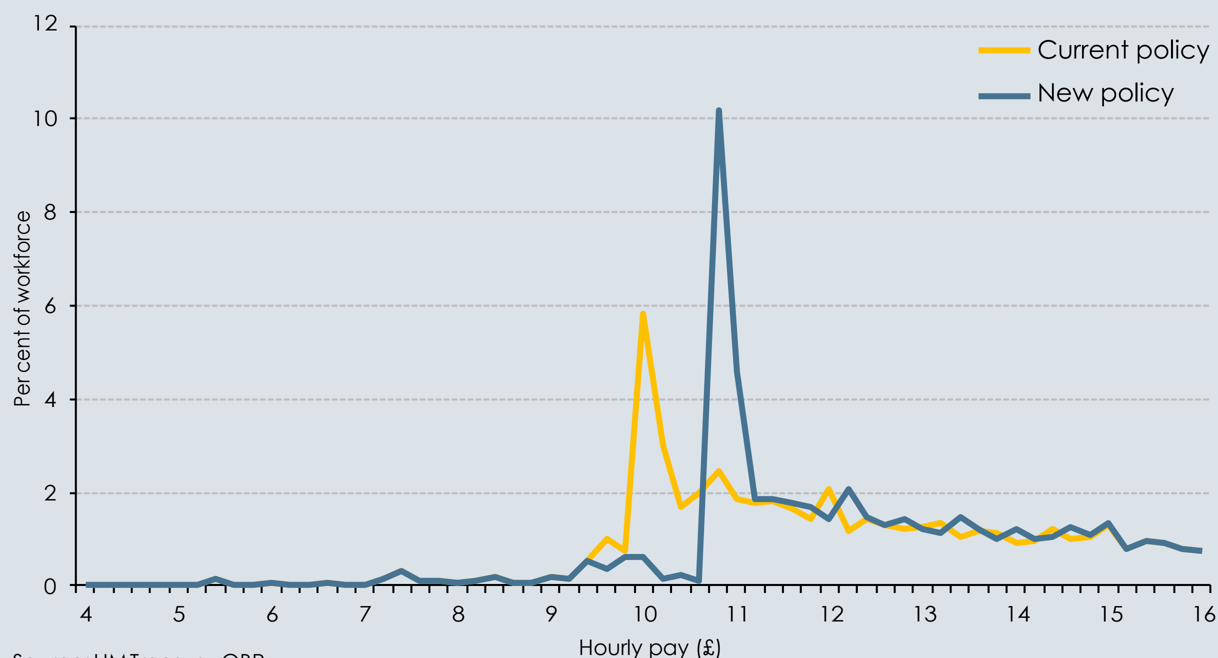

Source: HM Treasury calculations, OECD, ONS

The path that the NLW will take remains uncertain, as the rates themselves are set annually, informed by recommendations from by the Low Pay Commission. For the purposes of this forecast, we have assumed that the NLW will rise smoothly to reach the desired level in 2024.

We have estimated the economic effects of the increase using a similar framework to that we applied in July 2015 when the NLW was first announced, but reflecting the latest evidence:[a]

- We have retained our assumption that the impact of the NLW on earnings spills over to those with hourly earnings up to 40 per cent above the new NLW, as employers and employees seek to maintain wage differentials (Chart D).
- There is limited evidence that previous increases in the National Minimum Wage and NLW have had a significant impact on aggregate employment, so we have revised down our assumption of the responsiveness of total hours to increases in the NLW to an elasticity of 0.3 (from 0.4 previously). This remains somewhat higher than the literature might appear to suggest, reflecting the fact that the higher NLW will increasingly apply in sectors subject to conventional market pressures.

## Chart D: Illustrative earnings distributions in 2024




Source: HM Treasury, OBR

Using these assumptions, we estimate that the rise in the NLW will reduce total hours worked by 0.3 per cent, and that the effect is split evenly between unemployment and average hours worked. That corresponds to a rise in unemployment of around 50,000 (and an increase in our estimate of the equilibrium unemployment rate from 4.0 to 4.1 per cent) by 2024. As the loss of hours worked is concentrated at the bottom of the earnings distribution, there is an offsetting positive compositional (or 'batting average') effect on productivity. Overall, real GDP is 0.1 per cent lower than it would have been by 2024.

Table C shows how the higher path for the NLW has affected our fiscal forecast:

- The largest effect is on income tax and NIC receipts, which are up by £1.5 billion a year by 2024-25. This effect is much larger than our estimate at the time of the initial NLW announcement in July 2015 because around three-quarters of those benefiting earn more than the personal allowance and the primary and secondary thresholds for NICs. As a result, most of the additional earnings will be taxed at a higher marginal rate. This includes the effect of fewer hours and lower employment.
- As regards other receipts, the squeeze on profit margins lowers corporation tax receipts, while higher consumer spending adds modestly to VAT and excise duty receipts.
- The overall effect on welfare spending is close to zero, but this reflects offsetting effects. Higher earnings will reduce eligibility for means-tested benefits. But higher unemployment will add to spending on universal credit, while higher earnings growth will raise spending on state pensions via triple lock uprating. Other uprating effects will be small.
- Modestly higher RPI inflation adds to debt interest spending.

This does not include the additional costs for local authorities of providing adult social care.

### Table C: Fiscal effects of increasing the National Living Wage

| | £ billion | | | |
|---|---|---|---|---|
| | Forecast | | | |
| | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Total effect on net borrowing | -0.3 | -0.6 | -0.9 | -1.2 |
| *of which:* | | | | |
| Welfare spending | -0.1 | -0.1 | -0.1 | 0.0 |
| Earnings effects | -0.1 | -0.3 | -0.4 | -0.5 |
| Uprating effects | 0.0 | 0.1 | 0.3 | 0.4 |
| Unemployment effects | 0.0 | 0.1 | 0.1 | 0.2 |
| Income tax and NICs receipts | -0.4 | -0.8 | -1.1 | -1.5 |
| Corporation tax receipts | 0.1 | 0.1 | 0.2 | 0.2 |
| Other receipts | 0.0 | 0.0 | 0.0 | -0.1 |
| Debt interest | 0.2 | 0.2 | 0.2 | 0.2 |

[a] A. Dube, *Impacts of Minimum Wages: Review of the International Evidence*, 2019 and Low Pay Commission, *National Minimum Wage: Low Pay Commission Report*, 2019.
[b] For more detail see *More than a minimum: the review of the minimum wage*, Professor Sir George Bain, March 2014.

## Prospects for inflation

2.58 In assessing the outlook for the economy and the public finances, we are interested in several different measures of inflation, principally the Consumer Prices Index (CPI) and the Retail Prices Index (RPI). But we also need to forecast the GDP deflator and its components, which are required to generate a projection for nominal GDP.

2.59 CPI and RPI inflation affect the public finances in several ways. The Government uses the CPI to index many allowances and thresholds, and to uprate benefits and public service pensions. The RPI is no longer a National Statistic, because it falls short of agreed international statistical standards,[13] but the Government still uses it to calculate interest payments on index-linked gilts, interest charged on student loans and to revalorise excise duties. The ONS publishes several other inflation measures – most notably CPIH, a variant of the CPI that includes housing costs. But as these do not currently affect the public finances, we do not forecast them.

### CPI inflation

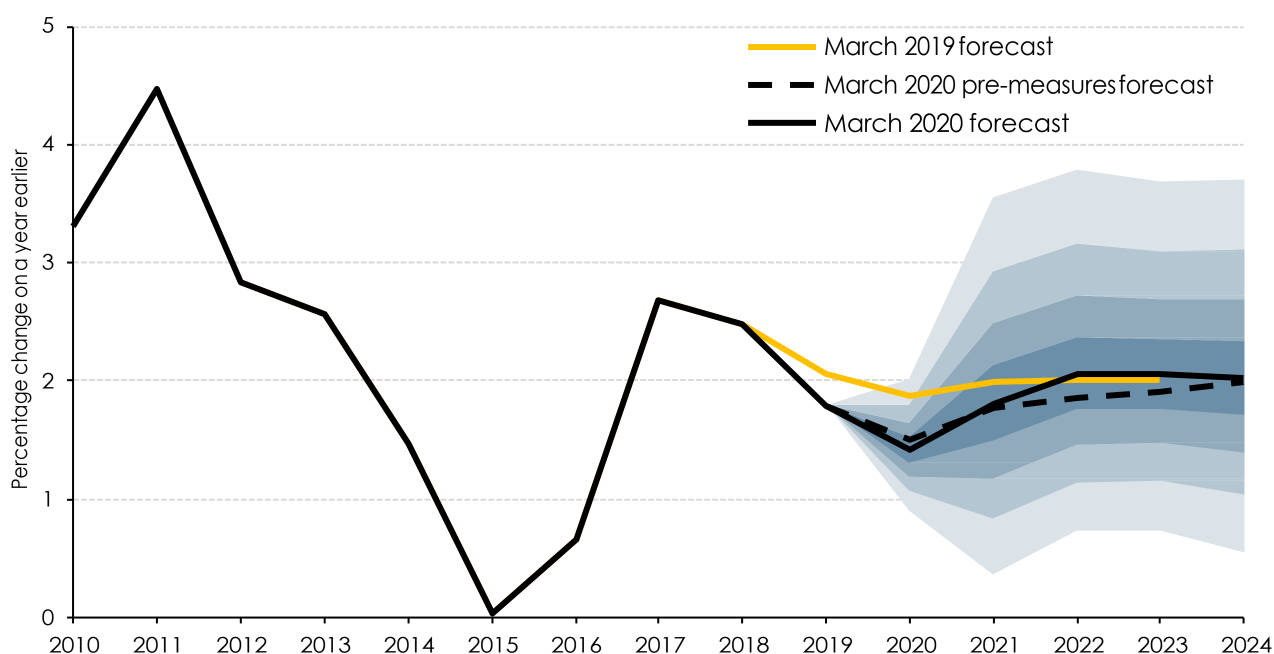
2.60 CPI inflation averaged 1.4 per cent in the fourth quarter of 2019, below the MPC's 2 per cent target and 0.6 percentage points lower than we forecast last March. We expect a tick up to 1.8 per cent in the first quarter of this year, partly due to the impact on the annual comparison of temporarily low energy and fuel prices a year ago. This is followed by a dip to 1.2 per cent in the second quarter, in part driven by the announced drop in the Ofgem energy price cap for April.

[13] ONS, *Shortcomings of the Retail Prices Index as a measure of inflation*, March 2018.

2.61 Several policy measures affect the inflation forecast (see Box 2.2). These include freezing alcohol duties, fuel duty and tuition fees, reintroducing the tobacco duty escalators and raising the National Living Wage. Fiscal easing also boosts economic activity and creates modest excess demand, placing some upward pressure on inflation and takes it slightly above target in 2022 and 2023. But we expect this effect to fade as a result of the higher paths for Bank Rate and sterling that we have assumed, so that inflation returns to the target by the end of the forecast period.

2.62 Chart 2.11 shows our latest central CPI inflation forecast within a fan chart produced using the same methodology that underpins the GDP fan chart (Chart 2.7). It illustrates the range of possible outcomes one would expect if past official forecast errors were a reasonable guide to future ones (which is not necessarily the case). It shows that the downward revisions to our forecast since March 2019 – mainly as a result of lower utility prices – are small compared to the historical differences between forecasts and outturns.

## Chart 2.11: CPI inflation fan chart




Source: ONS, OBR

## RPI inflation

2.63 RPI inflation averaged 2.2 per cent in the fourth quarter of 2019, 0.7 percentage points lower than our March forecast. We compile our RPI inflation forecast by adding a 'wedge' to our CPI inflation forecast for differences in measurement, coverage and weights. We have revised down the formula effect and weights component in the medium term in line with our revised assumptions for the wedge in the long run, outlined in Box 2.3 of our 2019 *FER*.[14]

[14] OBR, *Forecast evaluation report*, December 2019.

## The GDP deflator

2.64 The GDP deflator is a broad measure of prices in the domestic economy. It covers all goods and services that comprise GDP, including those relating to private and government consumption, investment and the relative price of exports to imports – the 'terms of trade'. GDP deflator inflation was estimated to be 1.8 per cent in 2019. We expect it to rise to a peak of 2.2 per cent in 2022 as CPI inflation rises to a slightly above-target rate and as increases in the growth in government spending raises the growth in the price of government consumption and investment. As public spending growth eases, we expect growth in government consumption prices to fall slightly and bring GDP deflator inflation back to 2.1 per cent by the end of the forecast period.

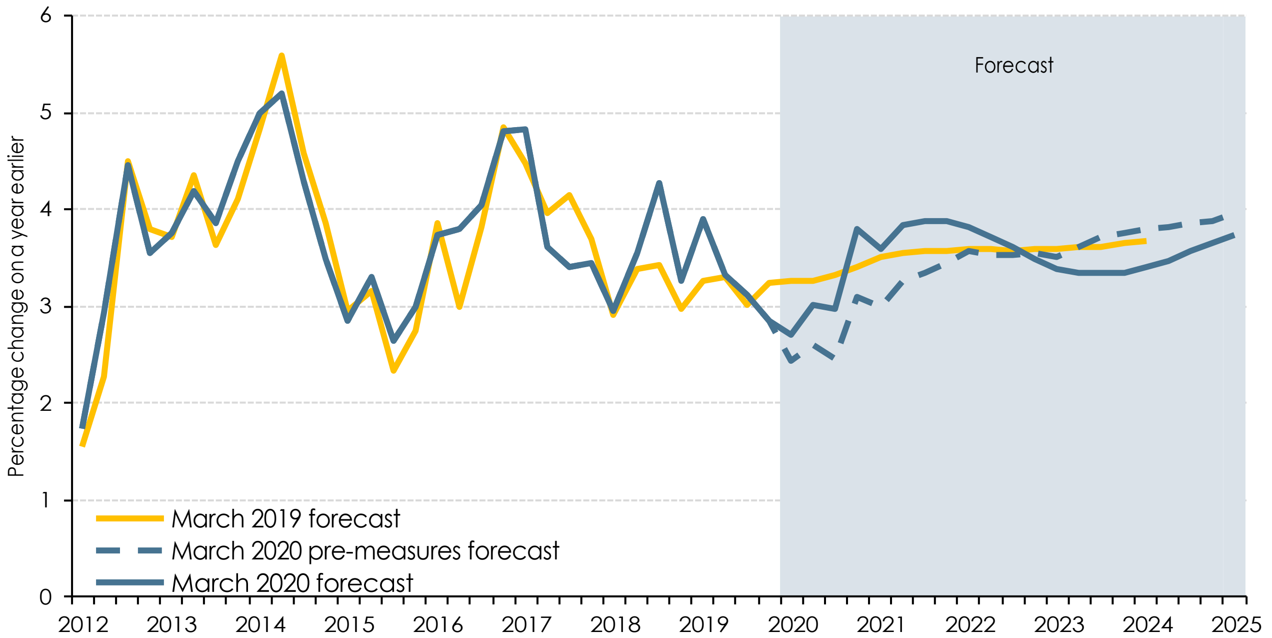
2.65 Overall, GDP deflator inflation is forecast to be higher than last March over the forecast period, mainly due to higher government consumption and investment inflation which result from the announced increase in government spending since last March.

## Prospects for nominal GDP

2.66 Most public discussion of the economic outlook focuses on real GDP – the volume of goods and services produced in the economy. But the nominal or cash value – and its composition by income and expenditure – is more important for the public finances. Taxes are driven primarily by nominal, rather than real, GDP. So too is the share of GDP devoted to public spending, as much of that spending is set out in multi-year cash plans (public services, grants and administrative, and capital spending) or linked to measures of inflation (including benefits, tax credits and interest on index-linked gilts).

2.67 We expect nominal GDP growth to slow in 2020 to 3.1 per cent from 3.3 per cent in 2019. This reflects weaker real GDP growth, which is partially offset by higher whole-economy inflation. We then expect nominal GDP growth to strengthen, peaking at 3.8 per cent in 2021, as real GDP growth picks up as a result of the fiscal easing, before slowing slightly in the remaining years of the forecast as the effects of the easing fade (Chart 2.12).

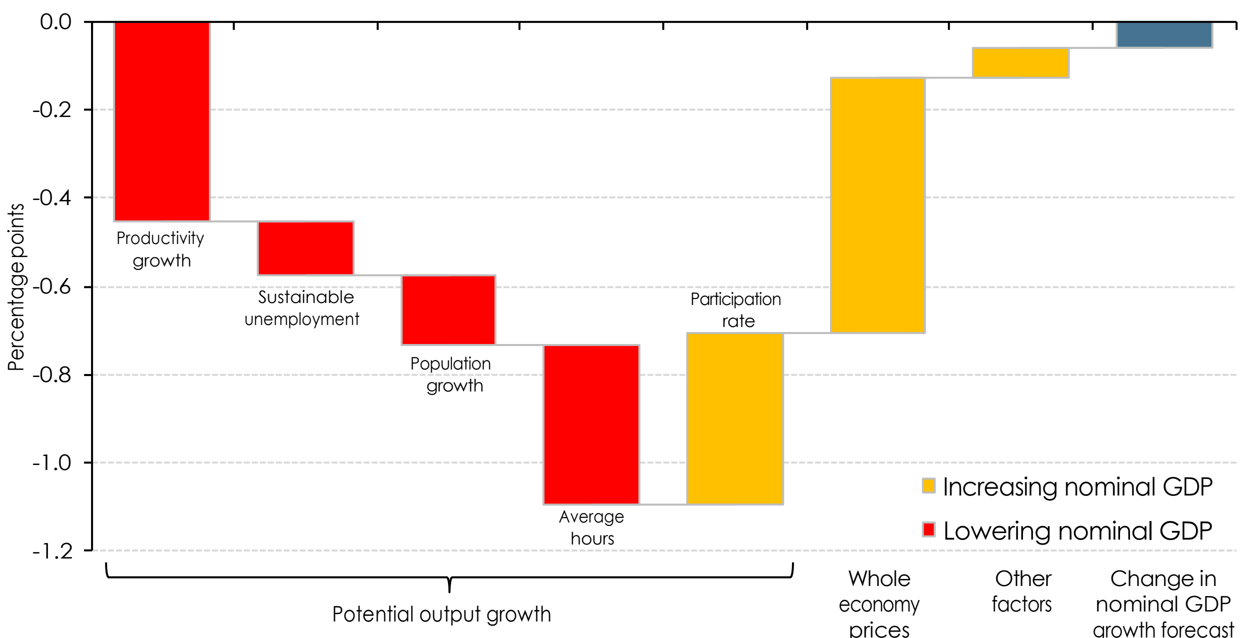
## Chart 2.12: Nominal GDP growth




Source: ONS, OBR

2.68 Cumulative nominal GDP growth between 2019-20 and 2023-24 is 14.9 per cent, the same as last March. But that masks offsetting revisions to output and inflation, shown in Chart 2.13. The permanent reduction in supply potential is offset by the inflationary consequences of the fiscal expansion, which delivers a permanent increase in the whole economy price level. The composition of that growth is also more 'tax-rich' than we predicted last March. In particular, cumulative wages and salaries growth is 0.4 percentage points higher; labour income is more heavily taxed than other forms of income or spending.

## Chart 2.13: Sources of revision to nominal GDP growth from 2019-20 to 2023-24

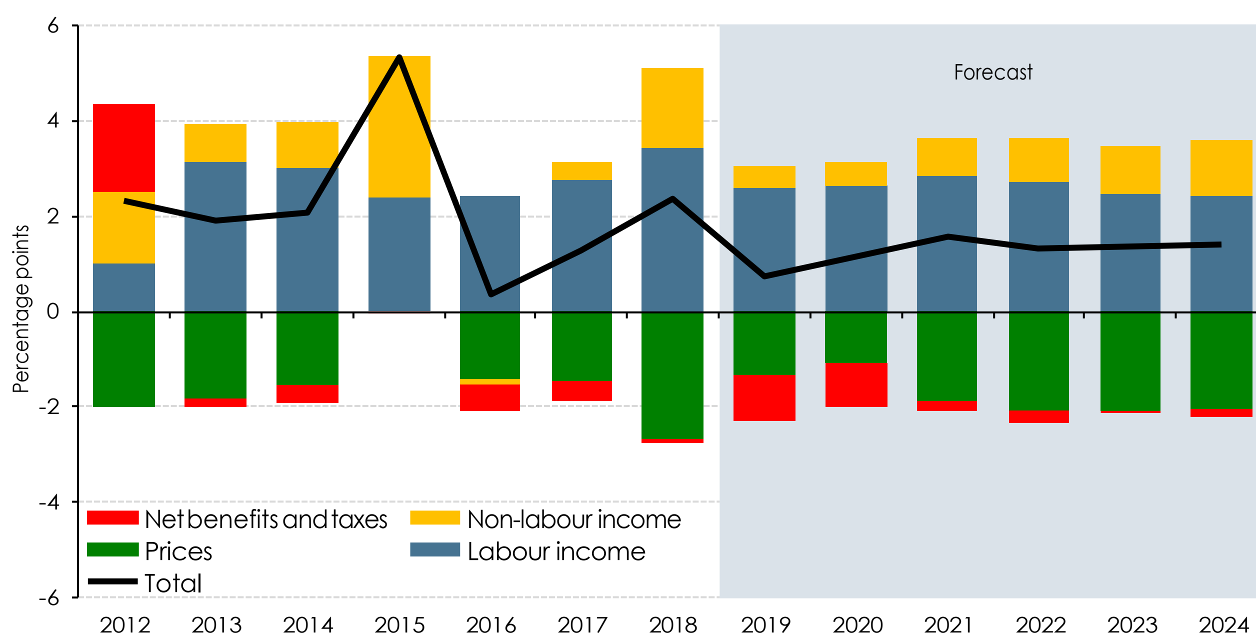



Source: OBR

## Income composition of GDP growth

2.69 Nominal household disposable income growth has slowed since 2018, with both labour and non-labour income decelerating and an increased drag from net benefits and taxes. We expect household income growth to edge up in 2020 and pick up further thereafter as non-labour income growth strengthens and the drag from net benefits and taxes lessens. Real household income growth is expected to slow less sharply in 2019 and 2020, as lower inflation partly offsets weaker nominal household income growth (Chart 2.14).

### Chart 2.14: Contributions to real household income growth




Source: ONS, OBR

2.70 Non-oil private non-financial corporation (PNFC) profits have been more buoyant than we expected. We now estimate that profits grew by 4.1 per cent in 2019, up from 3.1 per cent in 2018 and above our March forecast of 2.2 per cent. Profit growth then slows to below 3 per cent in 2020 and 2021, falling as a share of GDP as the labour share rises. Profit growth subsequently recovers as margins are rebuilt, somewhat reversing the earlier profits squeeze, though the increases in the National Living Wage weigh on profit growth.

# Individual sectors of the economy

## Property market

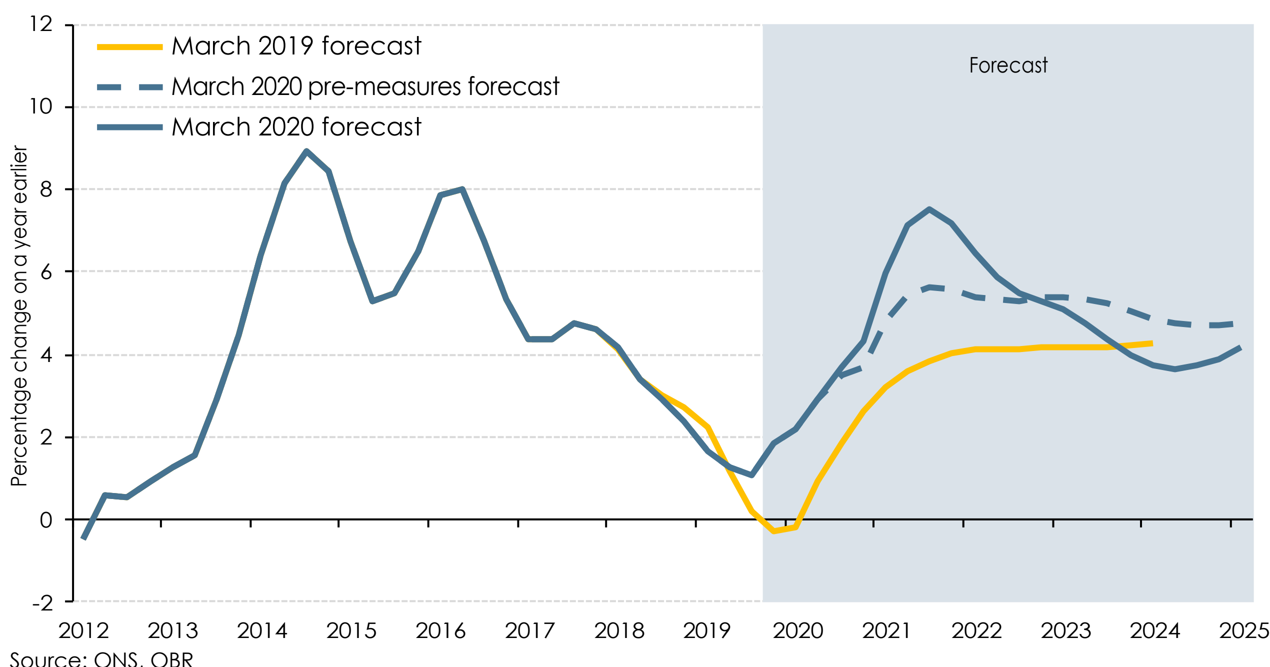
### Residential housing

2.71 House price inflation has slowed significantly in recent quarters. Having peaked in 2016 at 7.0 per cent, it fell steadily to reach 1.1 per cent in the third quarter of 2019. It has picked up slightly more recently, reaching 1.8 per cent in the fourth quarter of 2019.

2.72 Indicators of housing market activity and price expectations have shown signs of improvement since our March 2019 forecast and are consistent with higher house price inflation. The Halifax and Nationwide price indices – which are timelier than the ONS measure used in our forecast – have signalled a continued recovery. We expect annual house price inflation to reach 4.3 per cent by the end of 2020.

2.73 Beyond the near term, we expect house price inflation to pick up further as a result of stronger real household income growth (thanks partly to fiscal easing) and continued pressure of demand on supply (despite lower migration). We expect it to peak at 7.5 per cent in the third quarter of 2021, then to ease back to 4.1 per cent by the forecast horizon. Overall, we expect house prices to rise by 23 per cent between the fourth quarter of 2019 and the first quarter of 2024, up from 17 per cent in our previous forecast due to stronger real household income growth and lower interest rates.

## Chart 2.15: House price inflation forecast




Source: ONS, OBR

2.74 After increasing through 2018, residential property transactions fell in early 2019 – probably due to Brexit-related uncertainty and broadly in line with our March 2019 forecast. A slightly stronger rebound than we expected in the fourth quarter of 2019 meant that transactions ended the year 1.5 per cent higher than we anticipated. The latest near-term indicators of housing market activity point to this momentum being maintained and we expect transactions to rise by 4.5 per cent between the end of 2019 and the end of 2020. Thereafter, we expect transactions to continue rising gradually to a level that is similar to our March 2019 forecast by the end of 2024.

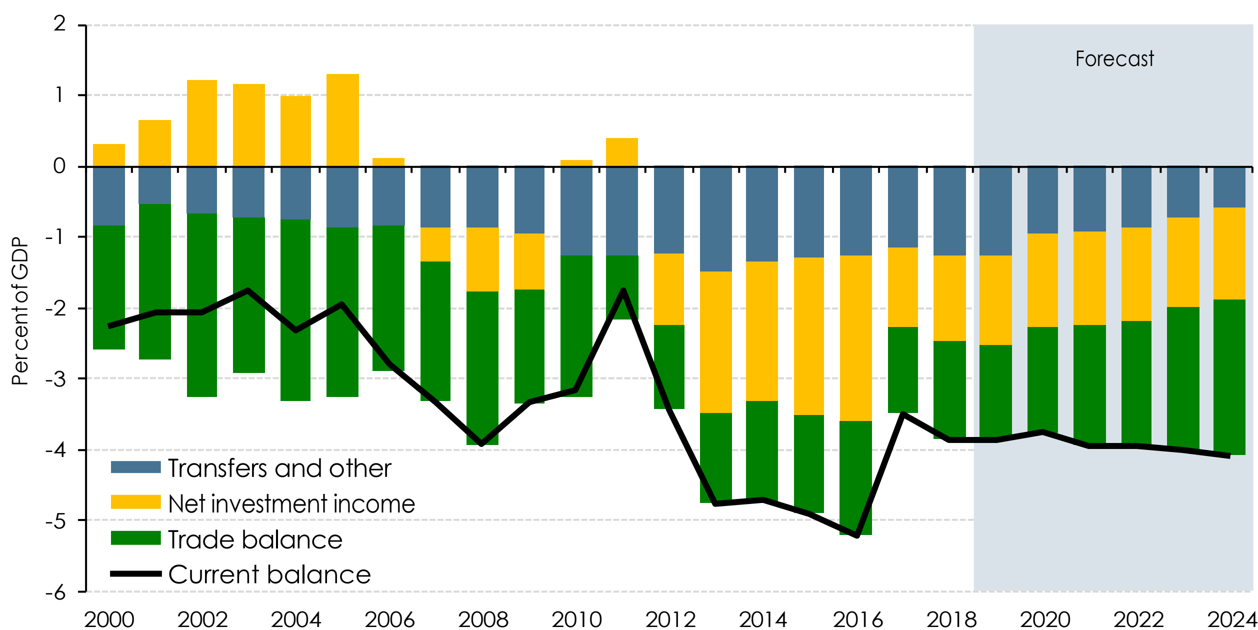
### Commercial property

2.75 Commercial property price inflation is expected to be lower in 2019-20 compared to our March 2019 forecast. In line with the consensus outlook from the IPF,[15] commercial property prices are expected to fall until 2021-22 before recovering in the remaining years. Our commercial property transactions forecast is weaker in 2019-20 compared to our previous forecast. Transactions are expected to fall until 2020-21 before recovering. These near-term changes reflect the latest outturn data from HMRC. The forecast is little changed thereafter.

## External sector

2.76 Over the past couple of years, the current account has on average been in deficit by around 4 per cent of GDP. The deficit narrowed in the third and fourth quarters of 2019 – driven by the trade deficit, although some of this related to trade in non-monetary gold. We expect the current account deficit to widen back to around 4 per cent of GDP by 2021, remaining around that level for the rest of the forecast. This widening is driven by the trade deficit which is partially offset by a narrowing of the transfers deficit, which reflects the declining path of EU financial settlement payments from 2021 onwards (Chart 2.16).

### Chart 2.16: Current account balance




Source: ONS, OBR

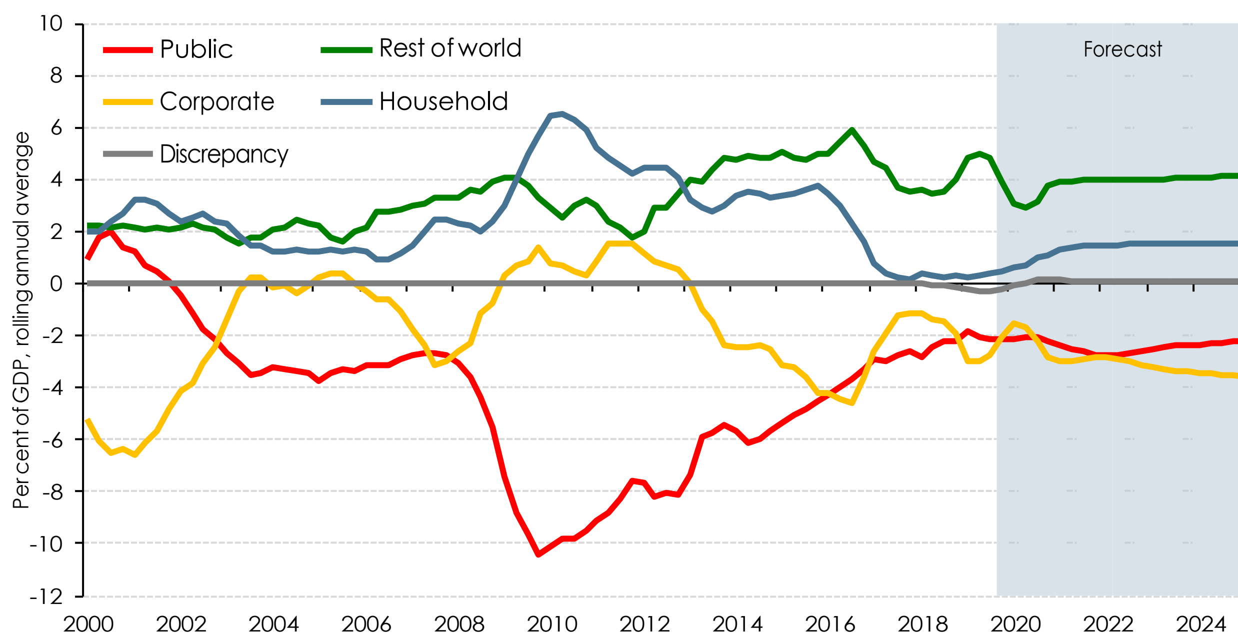
[15] Investment Property Forum, UK Consensus Forecasts Summer 2019.

## Sectoral net lending

2.77 In the National Accounts framework that underpins our economy forecast, the income and expenditure of the different sectors of the economy imply a path for each sector's net lending to, or borrowing from, the others. In practice, ONS estimates of sectoral net lending do not sum precisely to zero, reflecting differences between the income and expenditure measures of GDP (the 'statistical discrepancy'). Our standard practice is to assume that this difference remains flat over the forecast period from the most recent data.

2.78 In the first three quarters of 2019, households and the rest of the world were reported to be in surplus while the public and corporate sectors were in deficit. We expect the household sector surplus to widen as a share of GDP. This is offset by a wider corporate sector deficit (Chart 2.17).

### Chart 2.17: Sectoral net lending




Source: ONS, OBR

## Comparison with external forecasters

2.79 In this section, we compare our latest projections with those of selected outside forecasters. Our forecast incorporates the large fiscal package announced in the Budget. We do not know how much, if any, of the fiscal easing announced in the Budget may have been anticipated in those outside forecasts on the basis of the contents of the Conservative manifesto. We do know that the Bank of England's January 2020 *Monetary Policy Report* reflected the spending announcements made in Spending Round 2019 but – in line with its usual practice – did not make any allowance for what the Budget itself might include. None of the forecasts compared here take on board the recent developments in financial markets triggered by rising concerns about coronavirus.

2.80 In its January 2020 *Monetary Policy Report*, the Bank of England's modal forecast is for GDP to grow by 0.8 per cent in 2020 and 1.4 per cent in 2021. These are downwardly revised from its November *Report* and reflect expectations of a weaker near-term pick-up in potential output growth. For 2022, the Bank has a slightly more optimistic forecast for growth at 1.7 per cent, 0.2 percentage points higher than our own forecast. This pick-up in growth reflects expectations of a recovery in global activity and stronger domestic demand that together produce a small degree of cyclical overheating.

2.81 Table 2.5 compares our forecast for actual and potential output with the Bank's over the Bank's three-year forecast horizon. We expect potential output growth to be stronger than the Bank assumes due to differences in productivity forecasts. However, for actual output, our forecasts are similar. This is mainly because the Bank assumes that there is currently a higher margin of spare capacity (Table 2.6).

2.82 The Bank's modal CPI inflation forecast is largely the same as ours for most of their forecast period, only being slightly higher for 2021, as seen in Table 2.6. This is driven by stronger domestic price pressures as excess demand arises.

## Table 2.5: Potential and actual output comparisons against the Bank of England

| | Per cent | |
|---|---|---|
| | Average of four-quarter growth rates from Q1 2020-Q1 2023 | |
| | OBR | Bank of England |
| Potential output | 1.4 | 1.1 |
| *Main contributions:* | | |
| Productivity | 1.0 | 0.5 |
| Labour supply | 0.4 | 0.5 |
| Actual output | 1.4 | 1.4 |

Note: Components may not sum to total due to rounding.

## Table 2.6: Comparison with external forecasters

| | Per cent | | | | |
|---|---|---|---|---|---|
| | 2020 | 2021 | 2022 | 2023 | 2024 |
| OBR (March 2020) | | | | | |
| GDP growth | 1.1 | 1.8 | 1.5 | 1.3 | 1.4 |
| CPI inflation | 1.4 | 1.8 | 2.1 | 2.1 | 2.0 |
| Output gap | -0.1 | 0.4 | 0.4 | 0.2 | 0.0 |
| Bank of England (January 2020)[1] | | | | | |
| GDP growth (mode) | 0.8 | 1.4 | 1.7 | | |
| CPI inflation (mode)[2] | 1.4 | 2.0 | 2.1 | | |
| Excess demand/excess supply[3] | -0.5 | 0.3 | 0.5 | | |
| NIESR (February 2020)[4] | | | | | |
| GDP growth | 1.3 | 1.6 | 1.6 | 1.8 | 1.7 |
| CPI inflation | 1.8 | 2.1 | 2.0 | 2.0 | 2.0 |
| OECD (March 2020)[5] | | | | | |
| GDP growth | 0.8 | 0.8 | | | |
| CPI inflation | 2.0 | 1.8 | | | |
| Output gap | -1.1 | -1.2 | | | |
| IMF (January 2020)[6] | | | | | |
| GDP growth | 1.4 | 1.5 | 1.5 | 1.5 | 1.5 |
| CPI inflation | 1.9 | 2.0 | 2.0 | 2.0 | 2.0 |
| Output gap | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 |

[1] Forecast based on market interest rates.

[2] Fourth quarter year-on-year growth rate.

[3] Per cent of potential GDP.

[4] Output gap not published.

[5] The OECD updated GDP growth projections for 2020 and 2021 in their March 2020 *Interim Economic Outlook*. All other projections are from the November 2019 *Economic Outlook*.

[6] The IMF updated GDP growth projections for 2020 and 2021 in their January 2020 *WEO* update. All other projections are from the October 2019 *WEO*.

## Table 2.7: Detailed summary of forecast

| | Percentage change on a year earlier, unless otherwise stated | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
| UK economy | | | | | | | |
| Gross domestic product (GDP) | 1.3 | 1.4 | 1.1 | 1.8 | 1.5 | 1.3 | 1.4 |
| GDP per capita | 0.7 | 0.8 | 0.5 | 1.3 | 1.1 | 0.9 | 1.1 |
| GDP level (2018=100) | 100.0 | 101.4 | 102.5 | 104.3 | 105.8 | 107.1 | 108.6 |
| Nominal GDP | 3.5 | 3.3 | 3.1 | 3.8 | 3.7 | 3.4 | 3.5 |
| Output gap (per cent of potential output) | 0.2 | 0.1 | -0.1 | 0.4 | 0.4 | 0.2 | 0.0 |
| Expenditure components of GDP | | | | | | | |
| Domestic demand | 1.3 | 1.6 | 1.1 | 2.0 | 1.7 | 1.6 | 1.7 |
| Household consumption[1] | 1.6 | 1.3 | 1.1 | 1.2 | 1.2 | 1.4 | 1.4 |
| General government consumption | 0.4 | 3.6 | 3.7 | 2.8 | 2.1 | 1.9 | 2.2 |
| Fixed investment | -0.2 | 0.4 | -0.8 | 3.4 | 2.9 | 2.0 | 1.8 |
| Business | -1.5 | 0.3 | 0.0 | 1.8 | 3.0 | 2.4 | 2.3 |
| General government[2] | 1.3 | 2.1 | 1.9 | 10.9 | 4.6 | 1.8 | 1.2 |
| Private dwellings[2] | 6.5 | -0.3 | -4.2 | 1.5 | 1.6 | 1.3 | 1.2 |
| Change in inventories[3] | 0.2 | 0.1 | -0.1 | 0.1 | 0.0 | 0.0 | 0.0 |
| Exports of goods and services | 1.2 | 3.7 | -0.6 | -0.5 | -0.6 | -1.1 | -1.0 |
| Imports of goods and services | 2.0 | 3.6 | -0.2 | 0.4 | 0.2 | 0.2 | 0.2 |
| Balance of payments current account | | | | | | | |
| Per cent of GDP | -3.9 | -3.9 | -3.8 | -3.9 | -4.0 | -4.0 | -4.1 |
| Inflation | | | | | | | |
| CPI | 2.5 | 1.8 | 1.4 | 1.8 | 2.1 | 2.1 | 2.0 |
| RPI | 3.3 | 2.6 | 2.2 | 2.7 | 3.1 | 3.0 | 2.9 |
| GDP deflator at market prices | 2.2 | 1.8 | 2.0 | 2.0 | 2.2 | 2.1 | 2.1 |
| Labour market | | | | | | | |
| Employment (million) | 32.4 | 32.8 | 33.0 | 33.1 | 33.2 | 33.3 | 33.4 |
| Productivity per hour | 0.5 | 0.0 | 0.9 | 1.2 | 1.2 | 1.1 | 1.2 |
| Wages and salaries | 4.8 | 3.5 | 3.6 | 3.8 | 3.6 | 3.3 | 3.2 |
| Average earnings[4] | 3.3 | 2.8 | 3.3 | 3.6 | 3.4 | 3.1 | 3.1 |
| LFS unemployment (% rate) | 4.1 | 3.8 | 3.8 | 3.8 | 3.9 | 4.0 | 4.1 |
| Household sector | | | | | | | |
| Real household disposable income | 2.4 | 0.8 | 1.1 | 1.6 | 1.3 | 1.4 | 1.4 |
| Saving ratio (level, per cent) | 5.8 | 5.7 | 6.6 | 7.0 | 7.2 | 7.2 | 7.2 |
| House prices | 3.2 | 1.5 | 3.3 | 7.0 | 5.8 | 4.6 | 3.8 |
| World economy | | | | | | | |
| World GDP at purchasing power parity | 3.6 | 2.9 | 3.0 | 3.6 | 3.5 | 3.6 | 3.6 |
| Euro area GDP | 1.9 | 1.2 | 1.1 | 1.4 | 1.4 | 1.3 | 1.3 |
| World trade in goods and services | 3.7 | 1.1 | 1.9 | 3.9 | 3.6 | 3.7 | 3.8 |
| UK export markets[5] | 3.0 | 1.5 | 1.6 | 3.4 | 3.3 | 3.4 | 3.5 |

[1] Includes households and non-profit institutions serving households.

[2] Includes transfer costs of non-produced assets.

[3] Contribution to GDP growth, percentage points.

[4] Wages and salaries divided by employees.

[5] Other countries' imports of goods and services weighted according to the importance of those countries in the UK's total exports.

## Table 2.8: Detailed summary of changes to the forecast

| | Percentage point difference, unless otherwise stated | | | | | |
|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | |
| | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
| UK economy | | | | | | |
| Gross domestic product (GDP) | -0.1 | 0.2 | -0.4 | 0.2 | -0.1 | -0.3 |
| GDP per capita | 0.0 | 0.2 | -0.4 | 0.3 | 0.0 | -0.2 |
| GDP level (2018=100)[1] | 0.0 | 0.2 | -0.2 | -0.1 | -0.2 | -0.5 |
| Nominal GDP | 0.3 | 0.1 | -0.2 | 0.3 | 0.1 | -0.3 |
| Output gap (per cent of potential output) | 0.0 | 0.2 | 0.1 | 0.5 | 0.4 | 0.2 |
| Expenditure components of GDP | | | | | | |
| Domestic demand | -0.2 | -0.1 | -0.4 | 0.3 | 0.0 | -0.1 |
| Household consumption[2] | -0.1 | 0.2 | -0.4 | -0.4 | -0.4 | -0.2 |
| General government consumption | 0.2 | 1.4 | 2.0 | 1.2 | 0.5 | 0.2 |
| Fixed investment | -0.2 | -0.2 | -2.5 | 1.5 | 1.0 | -0.1 |
| Business | -0.6 | 1.3 | -2.4 | -0.5 | 0.6 | 0.0 |
| General government[3] | 0.7 | -3.8 | 0.0 | 8.7 | 3.6 | -0.2 |
| Private dwellings[3] | 0.9 | -1.3 | -4.6 | 1.2 | 0.1 | -0.3 |
| Change in inventories[4] | -0.1 | -0.4 | -0.1 | 0.1 | 0.0 | 0.0 |
| Exports of goods and services | 1.1 | 2.3 | -2.3 | -0.7 | -0.3 | -0.6 |
| Imports of goods and services | 1.2 | 0.6 | -2.3 | -0.2 | 0.2 | 0.1 |
| Balance of payments current account | | | | | | |
| Per cent of GDP | 0.4 | 1.2 | 1.3 | 1.0 | 0.8 | 0.7 |
| Inflation | | | | | | |
| CPI | 0.0 | -0.3 | -0.5 | -0.2 | 0.1 | 0.1 |
| RPI | 0.0 | -0.4 | -0.6 | -0.3 | 0.0 | -0.1 |
| GDP deflator at market prices | 0.4 | -0.1 | 0.2 | 0.1 | 0.2 | 0.1 |
| Labour market | | | | | | |
| Employment (million) | 0.0 | 0.2 | 0.2 | 0.2 | 0.2 | 0.1 |
| Productivity per hour | -0.1 | -0.8 | 0.0 | 0.1 | -0.1 | -0.2 |
| Wages and salaries | 0.4 | 0.1 | 0.3 | 0.3 | 0.2 | -0.2 |
| Average earnings[5] | 0.4 | -0.3 | 0.4 | 0.5 | 0.2 | -0.1 |
| LFS unemployment (% rate) | 0.0 | -0.3 | -0.3 | -0.2 | -0.1 | 0.0 |
| Household sector | | | | | | |
| Real household disposable income | 0.8 | 0.0 | 0.0 | -0.1 | -0.4 | -0.4 |
| Saving ratio (level, per cent) | 1.5 | 1.5 | 2.4 | 2.8 | 2.9 | 2.8 |
| House prices | -0.1 | 0.6 | 2.0 | 3.3 | 1.6 | 0.4 |
| World economy | | | | | | |
| World GDP at purchasing power parity | 0.0 | -0.6 | -0.6 | 0.0 | -0.1 | 0.0 |
| Euro area GDP | 0.1 | -0.4 | -0.6 | -0.2 | -0.1 | -0.1 |
| World trade in goods and services | -0.4 | -2.7 | -2.0 | 0.1 | -0.2 | 0.0 |
| UK export markets[6] | -0.9 | -1.9 | -1.9 | -0.1 | -0.2 | 0.1 |

[1] Per cent change since March 2019.
[2] Includes households and non-profit institutions serving households.
[3] Includes transfer costs of non-produced assets.
[4] Contribution to GDP growth, percentage points.
[5] Wages and salaries divided by employees.
[6] Other countries' imports of goods and services weighted according to the importance of those countries in the UK's total exports.

## Table 2.9: Determinants of the fiscal forecast

| | Percentage change on previous year, unless otherwise specified | | | | | | | Growth over forecast |
|---|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 | |
| GDP and its components | | | | | | | | |
| Real GDP | 1.6 | 1.1 | 1.3 | 1.7 | 1.4 | 1.3 | 1.5 | 8.5 |
| Nominal GDP[1] | 3.9 | 2.8 | 3.4 | 3.9 | 3.5 | 3.4 | 3.6 | 22.5 |
| Nominal GDP (£ billion)[1,2] | 2167 | 2229 | 2304 | 2394 | 2478 | 2562 | 2654 | 487 |
| Nominal GDP (centred end-March £bn)[1,3] | 2199 | 2263 | 2348 | 2437 | 2519 | 2606 | 2700 | 501 |
| Wages and salaries[4] | 4.2 | 3.5 | 3.8 | 3.6 | 3.7 | 3.2 | 3.3 | 23.1 |
| Non-oil PNFC profits[4,5] | 3.1 | 4.1 | 2.6 | 2.9 | 3.4 | 3.4 | 4.0 | 22.2 |
| Consumer spending[4,5] | 4.2 | 2.6 | 2.2 | 3.1 | 3.3 | 3.5 | 3.5 | 19.6 |
| Prices and earnings | | | | | | | | |
| GDP deflator | 2.1 | 1.9 | 2.0 | 2.1 | 2.1 | 2.1 | 2.1 | 13.0 |
| RPI | 3.1 | 2.6 | 2.1 | 2.9 | 3.0 | 2.9 | 2.8 | 17.6 |
| CPI | 2.3 | 1.8 | 1.4 | 1.9 | 2.1 | 2.0 | 2.0 | 11.7 |
| Average earnings[6] | 3.0 | 2.9 | 3.6 | 3.3 | 3.5 | 3.0 | 3.2 | 21.1 |
| 'Triple-lock' guarantee (September) | 2.6 | 4.0 | 3.2 | 3.7 | 3.4 | 3.2 | 3.0 | 22.3 |
| Key fiscal determinants | | | | | | | | |
| Employment (million) | 32.5 | 32.9 | 33.0 | 33.1 | 33.2 | 33.3 | 33.4 | 0.9 |
| Output gap (per cent of potential output) | 0.3 | 0.0 | 0.1 | 0.4 | 0.4 | 0.1 | 0.0 | -0.2 |
| Financial and property sectors | | | | | | | | |
| Equity prices (FTSE All-Share index) | 4003 | 4065 | 4245 | 4408 | 4565 | 4718 | 4888 | 885 |
| HMRC financial sector profits[1,5,8] | 1.9 | 1.5 | 1.7 | 1.9 | 1.8 | 1.7 | 1.8 | 10.8 |
| Residential property prices[9] | 2.6 | 1.6 | 4.2 | 7.1 | 5.4 | 4.2 | 3.9 | 29.4 |
| Residential property transactions (000s)[10] | 1192 | 1191 | 1259 | 1278 | 1317 | 1344 | 1373 | 181 |
| Commercial property prices[10] | 3.9 | -1.9 | -1.4 | 0.0 | 0.7 | 2.1 | 2.1 | 1.5 |
| Commercial property transactions[10] | -0.8 | -5.1 | -1.7 | 1.7 | 1.4 | 1.3 | 1.5 | -1.1 |
| Oil and gas | | | | | | | | |
| Oil prices ($ per barrel)[5] | 71.3 | 64.0 | 56.1 | 54.8 | 55.1 | 56.2 | 57.3 | -14.0 |
| Oil prices (£ per barrel)[5] | 53.4 | 50.1 | 42.1 | 40.6 | 40.6 | 41.3 | 41.9 | -11.5 |
| Gas prices (p/therm)[5] | 60.7 | 34.7 | 26.5 | 35.5 | 36.2 | 36.9 | 37.6 | -23.1 |
| Oil production (million tonnes)[5] | 50.9 | 51.6 | 51.0 | 48.3 | 45.9 | 43.6 | 41.5 | -9.3 |
| Gas production (billion therms)[5] | 13.6 | 13.0 | 13.0 | 12.4 | 11.8 | 11.2 | 10.7 | -2.9 |
| Interest rates and exchange rates | | | | | | | | |
| Market short-term interest rates (%)[11] | 0.8 | 0.8 | 0.8 | 0.8 | 0.9 | 0.9 | 0.9 | 0.1 |
| Market gilt rates (%)[12] | 1.4 | 0.8 | 0.9 | 0.9 | 0.9 | 1.0 | 1.1 | -0.3 |
| Euro/Sterling exchange rate (€/£) | 1.13 | 1.13 | 1.15 | 1.21 | 1.20 | 1.18 | 1.17 | 0.04 |

[1] Non-seasonally adjusted.
[2] Denominator for receipts, spending and deficit forecasts as a per cent of GDP.
[3] Denominator for net debt as a per cent of GDP.
[4] Nominal. [5] Calendar year.
[6] Wages and salaries divided by employees.
[7] Adjusted for timing effects.
[8] HMRC Gross Case 1 trading profits.
[9] Outturn data from ONS House Price Index.
[10] Outturn data from HMRC information on stamp duty land tax.
[11] 3-month sterling interbank rate (LIBOR).
[12] Weighted average interest rate on conventional gilts.

## Table 2.10: Changes in the determinants of the fiscal forecast

| | Percentage point difference, unless otherwise specified | | | | | | Growth over forecast |
|---|---|---|---|---|---|---|---|
| | Forecast | | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | |
| GDP and its components | | | | | | | |
| Real GDP | 0.1 | -0.1 | -0.2 | 0.1 | -0.2 | -0.3 | -0.8 |
| Nominal GDP[1] | 0.8 | -0.4 | 0.0 | 0.3 | -0.1 | -0.3 | -0.5 |
| Nominal GDP (£ billion)[1,2] | 37 | 29 | 30 | 39 | 38 | 33 | -3.7 |
| Nominal GDP (centred end-March £bn)[1,3] | 34 | 27 | 34 | 40 | 36 | 32 | -2.2 |
| Wages and salaries[4] | 0.1 | 0.3 | 0.3 | 0.1 | 0.3 | -0.4 | 0.8 |
| Non-oil PNFC profits[4,5] | 0.2 | 1.9 | -0.3 | -0.4 | -0.2 | -0.2 | 0.9 |
| Consumer spending[4,5] | 0.3 | -0.7 | -1.2 | -0.6 | -0.4 | -0.2 | -3.4 |
| Prices and earnings | | | | | | | |
| GDP deflator | 0.4 | -0.1 | 0.1 | 0.2 | 0.2 | 0.1 | 0.5 |
| RPI | -0.1 | -0.4 | -0.7 | -0.1 | 0.0 | -0.1 | -1.6 |
| CPI | 0.0 | -0.3 | -0.5 | -0.1 | 0.1 | 0.0 | -0.8 |
| Average earnings[6] | 0.1 | -0.1 | 0.5 | 0.2 | 0.3 | -0.3 | 0.8 |
| 'Triple-lock' guarantee (September) | 0.0 | 0.5 | 0.3 | 0.6 | 0.3 | 0.0 | 1.9 |
| Key fiscal determinants | | | | | | | |
| Employment (million) | 0.0 | 0.3 | 0.2 | 0.2 | 0.2 | 0.1 | 0.1 |
| Output gap (per cent of potential output) | 0.1 | 0.1 | 0.2 | 0.5 | 0.4 | 0.1 | 0.1 |
| Financial and property sectors | | | | | | | |
| Equity prices (FTSE All-Share index) | 2 | 135 | 181 | 200 | 206 | 201 | 199 |
| HMRC financial sector profits[1,5,8] | -1.3 | -1.6 | 0.0 | 0.1 | 0.0 | -0.1 | -1.7 |
| Residential property prices[9] | -0.3 | 1.4 | 2.1 | 3.2 | 1.3 | 0.0 | 9.1 |
| Residential property transactions (000s)[10] | -1 | 12 | 12 | -13 | -11 | -18 | -16.6 |
| Commercial property prices[10] | 0.3 | -0.3 | -0.5 | -1.9 | -1.3 | 0.1 | -3.9 |
| Commercial property transactions[10] | 0.7 | -6.3 | -3.2 | 0.1 | -0.2 | -0.4 | -10.3 |
| Oil and gas | | | | | | | |
| Oil prices ($ per barrel)[5] | 0.0 | 1.9 | -5.5 | -7.2 | -8.2 | -8.3 | -8.3 |
| Oil prices (£ per barrel)[5] | 0.0 | 2.4 | -4.4 | -5.7 | -6.0 | -5.8 | -5.8 |
| Gas prices (p/therm)[5] | 0.0 | -15.8 | -26.6 | -18.6 | -19.0 | -19.4 | -19.4 |
| Oil production (million tonnes)[5] | 3.6 | 3.2 | 2.6 | 2.3 | 2.2 | 2.1 | -1.5 |
| Gas production (billion therms)[5] | -0.1 | -0.7 | -0.3 | -0.2 | -0.2 | -0.2 | -0.1 |
| Interest rates and exchange rates | | | | | | | |
| Market short-term interest rates (%)[11] | 0.0 | -0.2 | -0.3 | -0.4 | -0.4 | -0.5 | -0.5 |
| Market gilt rates (%)[12] | 0.0 | -0.5 | -0.5 | -0.6 | -0.7 | -0.7 | -0.7 |
| Euro/Sterling exchange rate (€/£) | 0.00 | 0.00 | 0.03 | 0.10 | 0.10 | 0.10 | 0.10 |

[1] Non-seasonally adjusted.
[2] Denominator for receipts, spending and deficit forecasts as a per cent of GDP.
[3] Denominator for net debt as a per cent of GDP.
[4] Nominal. [5] Calendar year.
[6] Wages and salaries divided by employees.
[7] Adjusted for timing effects.
[8] HMRC Gross Case 1 trading profits.
[9] Outturn data from ONS House Price Index.
[10] Outturn data from HMRC information on stamp duty land tax.
[11] 3-month sterling interbank rate (LIBOR).
[12] Weighted average interest rate on conventional gilts.

# 3 Fiscal outlook

## Introduction

3.1 This chapter:

- specifies the assumptions that we have made in respect of the UK's exit from the EU (from paragraph 3.5);
- explains the effects of new policies announced since March 2019 on the fiscal forecast (from paragraph 3.8);
- reviews classification issues affecting our forecast (in paragraph 3.11);
- describes the outlook for public sector receipts, including a tax-by-tax analysis explaining how the forecasts have changed since March 2019 (from paragraph 3.18);
- portrays the outlook for public sector expenditure, focusing on spending covered by departmental expenditure limits and the components of annually managed expenditure, including those subject to the 'welfare cap' (from paragraph 3.23);
- presents the outlook for the key fiscal deficit aggregates, including headline and structural measures of the budget deficit (from paragraph 3.88);
- shows the outlook for key balance sheet aggregates, such as public sector net debt, and for government lending to the private sector and other financial transactions, including asset sales (from paragraph 3.108); and
- summarises risks and uncertainties, including those embodied in the reporting of contingent liabilities (paragraph 3.137).

3.2 Further breakdowns of receipts and expenditure and other details of our forecast are provided in extensive supplementary tables on our website. The forecasts in this chapter start from the estimates of 2018-19 outturn data published by the Office for National Statistics (ONS) on 21 February. We then present an in-year estimate for 2019-20 that makes use of ONS outturn data for April 2019 to January 2020 and limited administrative tax data for some of February. Finally, we present forecasts for 2019-20 to 2024-25.

3.3 The Foreword to this document describes the timetable that was followed in producing the forecasts presented here. As is usual, we closed our pre-measures economy and fiscal forecasts well ahead of the Budget to provide a stable base against which the Chancellor could assess his policy measures. The pre-measures economy forecast was closed on 18

February and the fiscal forecast on 25 February. And they reflect information gathered from financial market prices over the 10 days to 11 February. After that, the only changes relate to Budget measures and other policy announcements – in this forecast these include the new migration regime and the higher National Living Wage. Since we closed our pre-measures forecast, news about the spread of coronavirus has prompted unusually large movements in asset prices, while other forecasters have been reassessing the economic outlook to take on board the possible adverse economic consequences. The ultimate spread and economic impact of coronavirus are at this stage highly uncertain, but they represent a clear downside risk to the forecasts presented below. The consequences are, though, most likely to be concentrated in the near term. We discuss the coronavirus-related risks to our economy forecast in Box 2.3 and associated fiscal risks in this chapter.

3.4 As in previous *Economic and fiscal outlooks (EFOs)*, this fiscal forecast:

- Represents our central view of the path of the public finances, based on the current policies and policy assumptions of the Government, and the information and conditioning assumptions that we thought appropriate when compiling our pre-measures forecast in mid-February. On that basis, we believed that, in the absence of future policy or classification changes, the outturns were as likely to be above the forecast as below it. But the near-term risks to economic activity have since clearly pivoted to the downside.
- Is based on announced Government policy on the indexation of rates, thresholds and allowances for taxes and benefits, and incorporates estimates of the effects of new policies announced since our previous forecast in March 2019.
- Focuses on official 'headline' fiscal aggregates that exclude public sector banks.

## Assumptions regarding the UK's exit from the EU

3.5 The OBR is required by legislation to produce its forecasts based on current government policy (but not necessarily assuming that particular policy objectives will be met). With negotiations over the UK's future relationship with the EU still taking place, this is not straightforward. We asked the Government to provide any additional information on its policies regarding Britain's departure from the EU that would be relevant to our forecasts.

3.6 The Government directed us to the Prime Minister's speech on 3 February[1] and to a paper published on 27 February[2] setting out the Government's proposed approach to negotiations about the future relationship with the EU. The Government also issued a public consultation on amendments to the tariffs currently applied through the EU's Common External Tariff,[3] which closed on 5 March. On 19 February the Government published an immigration policy statement, setting out the Government's intended immigration regime after the end of

[1] Prime Minister's Office and The Rt Hon Boris Johnson MP, *PM speech in Greenwich: 3 February 2020*, February 2020.
[2] Prime Minister's Office, *Our approach to the Future Relationship with the EU*, February 2020.
[3] Department for International Trade, *The UK Global Tariff*, February 2020.

the transition period.[4] We have reflected the new migration regime in this forecast, whereas other areas remain subject to the continuing negotiations between the UK and the EU, or to future UK Government policy decisions.

3.7 In addition to the potential future trade and migration regimes, there are several areas where the Government's post-transition policy objective is clear, but we have needed to make auxiliary assumptions to construct our fiscal forecast. For example:

- We assume there are no changes to the structure or effectiveness of tax systems for which there are common EU rules, such as VAT, unless otherwise stated.
- The Treasury is still considering responses to its recently concluded consultation on the UK's new 'Most Favoured Nation' tariff schedule. Our customs duty forecast therefore assumes that the regime that is presently in operation will continue; any subsequent changes will be reflected in a future forecast and costed relative to that baseline.
- There is no further information regarding fee status and eligibility for student finance for EU students beyond the 2020-21 academic year. We therefore assume that the forecast for EU-domiciled student entrants will be stable from the academic year 2020-21.
- The Government has promised to pursue an approach to vehicle emissions regulation "*at least as ambitious*"[5] as the current arrangements and a system of carbon pricing of "*at least the same effectiveness and scope*" as the EU emissions trading system. In the absence of firm policies in these areas, we assume the EU schemes continue, consistent with the stated position that UK replacement schemes will be at least equivalent in effect.

## Policy announcements

3.8 The Government has announced a large Budget giveaway, with public spending being placed on a much higher path than the previous plans embodied in our March 2019 forecast. It has financed this in part with the direct fiscal savings associated with Brexit – the contributions no longer required (net of the divorce settlement) and the customs duties no longer remitted to the EU – and by cancelling the corporation tax cut that was due in April 2020. But, for the most part, higher spending is financed through higher borrowing.

3.9 The large and sustained fiscal easing provides a temporary boost to real economic activity and leaves the cash size of the economy permanently larger via its effects on whole-economy inflation. This boosts all the major tax bases, raising receipts. The effect of the Budget package on borrowing and interest rates raises debt interest spending. And since more than one pound in ten of higher departmental current spending goes on pension contributions, the medium-term net cost of public service pensions is reduced materially.

[4] Home Office, *The UK's points-based immigration system: policy statement*, February 2020.
[5] Office for Low Emission Vehicles, *The Road to Zero*, September 2018.

3.10 The new migration regime raises borrowing by reducing population and receipts growth, but the effect is tempered by the foregone population growth being concentrated amongst the lower paid, reducing means-tested welfare spending and limiting the effect on income tax. A higher path for the National Living Wage reduces borrowing slightly.

## Table 3.1: Summary of the effect of Government decisions on the budget balance

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Total effect of Government decisions | 0.6 | -12.3 | -24.0 | -22.5 | -25.4 | -29.1 |
| Direct effect of policies on the scorecard | 0.6 | -17.9 | -36.4 | -38.5 | -41.2 | -41.9 |
| *of which:* | | | | | | |
| RDEL spending[1] | -2.5 | -14.9 | -27.2 | -31.9 | -35.6 | -38.6 |
| CDEL spending[1] | 0.0 | -7.0 | -16.7 | -19.2 | -20.0 | -20.7 |
| Use of direct Brexit fiscal savings | 0.0 | 4.3 | 5.0 | 7.1 | 11.3 | 14.6 |
| Receipts | 1.0 | 1.4 | 3.8 | 7.1 | 7.6 | 7.5 |
| Other AME spending | 2.1 | -1.6 | -1.3 | -1.7 | -4.4 | -4.7 |
| Direct effect of non-scorecard policies | 0.0 | 2.3 | 5.3 | 6.3 | 7.4 | 5.6 |
| *of which:* | | | | | | |
| RDEL spending[1] | -0.4 | -0.3 | 0.2 | 0.6 | 0.6 | -0.3 |
| CDEL spending[1] | 0.5 | 1.3 | 3.3 | 3.8 | 3.9 | 4.1 |
| Receipts | 0.0 | 0.6 | 0.9 | 0.9 | 1.0 | 1.0 |
| AME spending | 0.0 | 0.6 | 1.0 | 1.0 | 1.9 | 0.8 |
| Indirect effect of Government decisions | 0.0 | 3.3 | 7.1 | 9.7 | 8.4 | 7.2 |
| Total effect of Government decisions | 0.6 | -12.3 | -24.0 | -22.5 | -25.4 | -29.1 |
| *of which:* | | | | | | |
| Gross tax increases | 1.4 | 6.8 | 9.0 | 11.7 | 12.5 | 12.5 |
| Gross tax cuts | -0.4 | -4.8 | -4.3 | -3.7 | -3.9 | -3.9 |
| Total RDEL spending changes[1] | -2.9 | -15.2 | -27.0 | -31.2 | -34.9 | -38.9 |
| Total CDEL spending changes[1] | 0.5 | -5.7 | -13.4 | -15.4 | -16.1 | -16.7 |
| Total AME spending changes | 2.1 | 3.3 | 4.7 | 6.5 | 8.7 | 10.7 |
| Indirect effects | 0.0 | 3.3 | 7.1 | 9.7 | 8.4 | 7.2 |
| *of which:* | | | | | | |
| Due to tax and spending measures | 0.0 | 3.4 | 7.2 | 9.7 | 8.3 | 7.0 |
| Raising the National Living Wage | 0.0 | 0.0 | 0.3 | 0.6 | 0.9 | 1.2 |
| New migration regime | 0.0 | 0.0 | -0.3 | -0.5 | -0.8 | -1.0 |

[1] The change in 2024-25 is relative to a baseline that assumes DEL would otherwise have remained constant as a share of GDP.
Note: The full breakdown of this table can be found in Annex A. This table uses the Treasury scorecard convention that a positive figure means an improvement in PSNB, PSNCR and PSND.

## Classification and other statistical changes

3.11 In December 2019 we restated our March 2019 forecast to reflect the significant changes introduced by the ONS in September 2019.[6] These included changes to the treatment of student loans, funded public sector pensions, depreciation and corporation tax credits. Since then, the ONS has announced the classification of Pool Re (a terrorism reinsurer) to the central government sector, but has not yet provided estimates of the effect this will have on the public finances. As such we are unable to include Pool Re in this forecast.

[6] OBR, *Restated March 2019 forecast,* December 2019

3.12 The Government has announced several measures in this Budget that the ONS will in due course need to classify. Pending these decisions, and reflecting the advice of Treasury classification experts, we have assumed that:

- the new plastic packaging tax is a tax on production;
- a green gas levy on suppliers to the gas grid is a tax on production and the corresponding payment to producers of biomethane is a subsidy;
- a UK scheme to replace the EU fines on car manufacturers for excess $CO_2$ emissions in their new car sales will accrue at the point the emissions are reported;
- Brexit financial settlement payments to the EU will accrue when the UK receives twice-yearly communication from the EU as to the amounts due; and
- changes to the payment date for some import VAT liabilities will affect cashflows but not the accrued recording of VAT receipts.

3.13 In addition, we have changed the way in which we show the effect of customs duties being retained by the Exchequer from the end of 2020, when the Brexit transition period ends. In our previous post-referendum forecasts, the move from them being recorded as an EU tax to being a UK tax was subsumed within our fiscally neutral assumption that direct savings from leaving the EU would finance other public spending. With DEL envelopes for the next Spending Review being set at this Budget, we now record the customs duty receipts as they will appear in reality and have increased spending accordingly (see Box 3.5). This better reflects the real-world position on both receipts and spending without altering our fiscally neutral assumption that direct fiscal savings related to Brexit will be spent. This assumption has in effect been confirmed by the higher DEL spending announced in the Budget

3.14 The ONS is considering several issues that could materially affect future forecasts. Some relate to things that have been included in this forecast:

- the classification of two previously announced policies that we have provisionally recorded as taxes: the apprenticeship levy and the digital services tax; and
- the sale of railway arches and spectrum licences, which we include as financial transactions affecting debt immediately with smaller flow effects on the deficit.

3.15 Others relate to things that we have not anticipated in this forecast:

- the classification or recording of the Nuclear Liabilities Fund, which could have implications for both the balance sheet and the deficit; and
- the implications for the public finances of a change to the recording of leases in commercial accounts (under the 'IFRS 16' accounting standard).

3.16 The change to leases could be significant. Currently *finance* leases are recorded on the balance sheet of the lessee, whereas for *operating* leases the asset remains on the lessor's. Under IFRS 16, nearly all leases will be reported on the balance sheet within lessees' financial statements, leading to increases in their reported debt and non-current assets.

3.17 The ONS has concluded that for property leases IFRS 16 is a good proxy for the ESA10 accounting standard used for the public finances, but that a modified IFRS 16 dataset will be needed for other leases.[7] It is now working to establish appropriate data and aims to introduce changes this autumn. The ONS has not released estimates of the scale of the impacts, so we are unable to anticipate them in this forecast. But the changes are likely to increase substantially the number of finance leases on the Government's books, raising measured debt, capital spending and depreciation, but reducing rental payments on operating leases that are part of current spending. Given the enormous number of leases the public sector engages in – the Treasury estimates there to be around 55,000 in central government alone – the impacts could be large. Prompted by this change in treatment, it is possible that departments might reconsider whether the contracts should be leases at all. The effect of this on the public finances is also uncertain.

## Public sector receipts

3.18 Table 3.2 summarises our receipts forecast. Receipts rise relative to GDP in every year, reflecting several revenue-raising policies, as well as underlying growth in our forecasts. Income tax and NICs rise by 0.2 per cent of GDP in 2020-21, because unchanged personal allowance and higher rate thresholds mean that more people are dragged into higher tax bands. Removing eligibility to use cheaper 'red diesel' from most current users boosts fuel duty by 0.1 per cent of GDP in 2022-23. Capital taxes rise strongly over the forecast, benefitting from underlying growth in equity and house prices, as well as our assumption that effective tax rates will rise. They are boosted from 2021-22 onwards by the restriction of entrepreneur's relief announced in the Budget.

[7] ONS, *Looking ahead – developments in public sector finance statistics: 2019*, May 2019

## Table 3.2: Major receipts as a share of GDP

| | Per cent of GDP | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Income tax | 8.9 | 8.8 | 9.0 | 9.1 | 9.2 | 9.2 | 9.3 |
| NICs | 6.3 | 6.5 | 6.5 | 6.6 | 6.6 | 6.6 | 6.7 |
| Value added tax | 6.1 | 6.1 | 6.1 | 6.1 | 6.1 | 6.1 | 6.1 |
| Onshore corporation tax | 2.5 | 2.4 | 2.5 | 2.5 | 2.5 | 2.5 | 2.5 |
| Fuel duties | 1.3 | 1.2 | 1.2 | 1.2 | 1.2 | 1.2 | 1.2 |
| Business rates | 1.4 | 1.4 | 1.4 | 1.4 | 1.4 | 1.4 | 1.4 |
| Council tax | 1.6 | 1.6 | 1.6 | 1.6 | 1.6 | 1.6 | 1.6 |
| Alcohol and tobacco duties | 1.0 | 0.9 | 0.9 | 0.9 | 0.9 | 0.9 | 0.8 |
| Capital taxes[1] | 1.4 | 1.4 | 1.5 | 1.5 | 1.6 | 1.7 | 1.8 |
| UK oil and gas receipts | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other taxes | 3.3 | 3.4 | 3.4 | 3.3 | 3.3 | 3.3 | 3.3 |
| National Accounts taxes | 33.9 | 33.9 | 34.1 | 34.2 | 34.4 | 34.5 | 34.6 |
| Interest and dividend receipts | 1.1 | 1.2 | 1.2 | 1.2 | 1.2 | 1.3 | 1.3 |
| Other receipts | 2.5 | 2.5 | 2.6 | 2.7 | 2.6 | 2.6 | 2.6 |
| Current receipts | 37.5 | 37.7 | 37.9 | 38.0 | 38.3 | 38.4 | 38.5 |

[1] Includes capital gains tax, inheritance tax, property transaction taxes and stamp taxes on shares.

### Sources of change in the receipts-to-GDP ratio

3.19 Movements in the receipts-to-GDP ratio can arise from two sources:

- changes in the composition of GDP can lead to specific tax bases growing more or less quickly than GDP as a whole; and

- the effective tax rate paid on each tax base can change due to policy or other factors.

3.20 Similar splits apply for non-tax receipts – for example, when considering movements in the receipts-to-GDP ratio due to interest and dividends, the split between changes in the government's asset holdings and in the effective interest rates earned on them.

### Change in the receipts-to-GDP ratio over the forecast period

3.21 The receipts-to-GDP ratio rises by 0.9 per cent of GDP between 2019-20 and 2024-25 to reach 38.5 per cent of GDP, the highest since the mid-1980s. National Accounts taxes rise to 34.6 per cent of GDP by the end of the forecast, the highest since 1969-70. These rises are more than explained by higher effective tax rates (due to policy measures and fiscal drag), which are partly offset by the composition of GDP becoming less tax rich. Chart 3.1 shows the contributions to the predicted rise in the receipts-to-GDP ratio.

3.22 The largest positive contributions to the change are:

- A 0.7 per cent of GDP rise in income tax and NICs receipts. Total income remains relatively flat as a share of GDP over the forecast, so the increase is entirely explained by the effective tax rate rising. This includes a 0.2 per cent of GDP rise in 2020-21 due to policy measures, in particular the Budget 2018 measure to hold the personal

allowance and higher rate threshold flat in that year (having raised them substantially in 2019-20). The remainder reflects fiscal drag, as a modest pick-up in the growth of productivity and real earnings pulls more income into higher tax brackets.

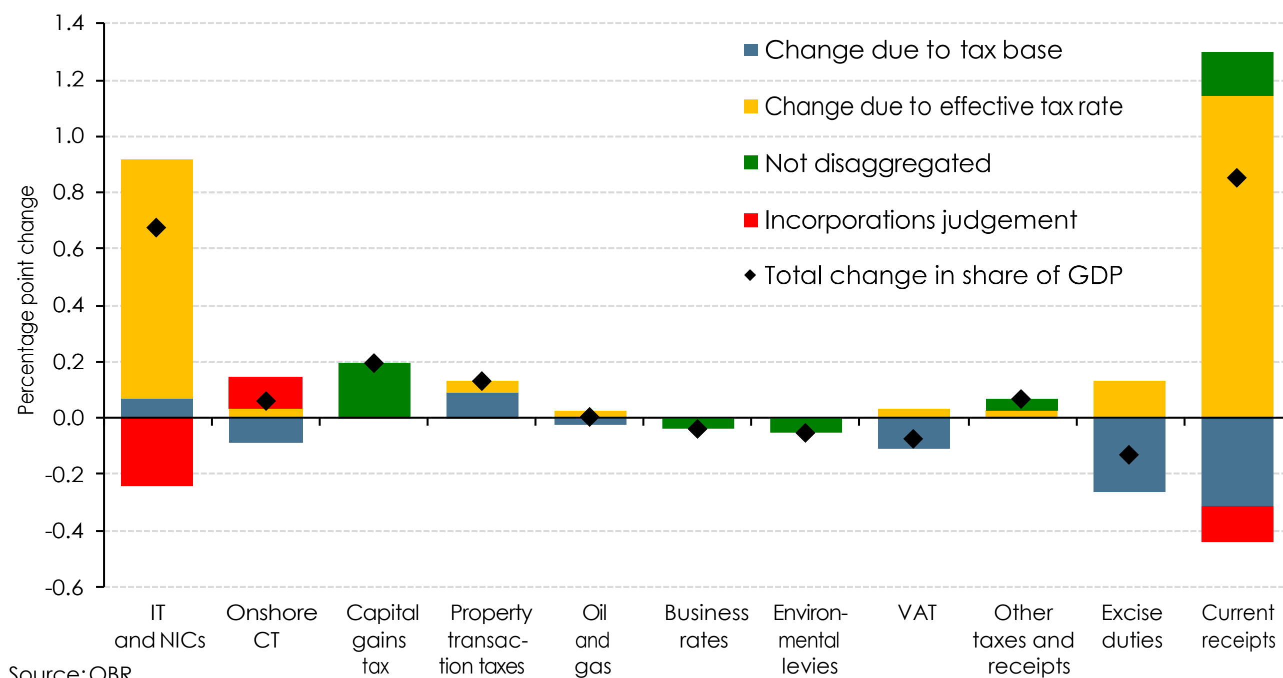
- A 0.1 per cent of GDP rise in onshore corporation tax. Most of this rise reflects our assumption that incorporations will continue to rise (though the negative effect of this on income tax and NICs receipts is greater[8]). Abstracting from incorporations, receipts rise by less than 0.1 per cent of GDP across the forecast. The positive impact from falling use of reliefs and deductions (in part explained by the annual investment allowance being cut from £1 million to £200,000 in January 2021) is offset by our assumption of subdued growth in financial company profits over the forecast.

3.23 The remaining upward contributions largely reflect taxes on capital, including property transaction taxes and capital gains tax (CGT). We assume that both equity and property prices rise over the forecast, boosting the tax base. Effective tax rates also rise thanks to fiscal drag in the property transaction tax system (as most thresholds remain flat over time) as well as our assumption that CGT receipts are geared to equity price gains (partly reflecting the tax system, which taxes the gain rather than the overall value of the disposal). (These forecasts are particularly sensitive to coronavirus risks to asset prices.)

3.24 The main offsetting fall reflects excise duties, which fall by 0.1 per cent of GDP between 2019-20 and 2024-25. This is explained by declining tax bases, due to trends in alcohol and tobacco consumption and rising fuel efficiency. These are only partly offset by rises in duty rates based on the Government's stated policy assumptions (which continue to assume increases in fuel duty from next year), but which has in practice been frozen every year since 2011-12) that raise the effective tax rate. The decision to restrict eligibility for 'red diesel' tempers the overall decline, adding 0.1 per cent of GDP to receipts in 2024-25.

[8] See Box 4.1 of our November 2016 *EFO* for more information.

## Chart 3.1: Sources of change in the tax-to-GDP ratio (2019-20 to 2024-25)




Source: OBR

## Detailed current receipts forecasts

3.25 Our detailed receipts forecasts and changes since March 2019 are presented in Tables 3.3 and 3.4. Further breakdowns are available on our website. Our forecasts for Scottish and Welsh devolved taxes are discussed in our *Devolved tax and spending forecasts* publication.

## Table 3.3: Current receipts

| | £ billion | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Income tax[1] | 192.6 | 195.2 | 207.5 | 217.4 | 227.3 | 236.6 | 246.6 |
| *of which:* Pay as you earn | 163.5 | 165.3 | 175.5 | 184.3 | 193.3 | 201.0 | 209.7 |
| Self assessment | 31.5 | 32.3 | 34.3 | 35.9 | 37.2 | 38.9 | 40.5 |
| Other income tax | -2.4 | -2.4 | -2.2 | -2.8 | -3.2 | -3.4 | -3.6 |
| National insurance contributions | 137.3 | 145.4 | 150.2 | 157.0 | 164.0 | 170.3 | 177.1 |
| Value added tax | 133.1 | 136.6 | 140.6 | 145.9 | 151.0 | 155.8 | 160.7 |
| Corporation tax[2] | 56.3 | 55.1 | 58.1 | 60.0 | 62.6 | 64.9 | 67.2 |
| *of which:* Onshore | 54.4 | 54.0 | 57.2 | 58.9 | 61.4 | 63.6 | 66.0 |
| Offshore | 1.9 | 1.1 | 0.9 | 1.1 | 1.1 | 1.2 | 1.2 |
| Petroleum revenue tax | -0.7 | -0.4 | -0.3 | -0.3 | -0.2 | -0.2 | -0.2 |
| Fuel duties | 28.0 | 27.7 | 27.5 | 28.1 | 30.5 | 31.2 | 31.7 |
| Business rates | 30.6 | 31.2 | 31.5 | 33.4 | 34.3 | 34.9 | 36.2 |
| Council tax | 34.8 | 36.2 | 37.9 | 39.1 | 40.3 | 41.6 | 42.9 |
| VAT refunds | 18.3 | 19.2 | 20.2 | 21.0 | 21.8 | 22.5 | 23.7 |
| Capital gains tax | 9.2 | 10.0 | 11.4 | 12.7 | 14.3 | 15.7 | 17.0 |
| Inheritance tax | 5.4 | 5.1 | 5.5 | 5.9 | 6.3 | 6.7 | 7.1 |
| Property transaction taxes[3] | 12.9 | 12.8 | 13.8 | 14.7 | 16.2 | 17.4 | 18.7 |
| Stamp taxes on shares | 3.6 | 3.4 | 3.6 | 3.7 | 3.9 | 4.0 | 4.1 |
| Tobacco duties | 9.2 | 8.7 | 9.0 | 8.8 | 8.8 | 8.7 | 8.7 |
| Alcohol duties | 12.1 | 12.1 | 11.9 | 12.4 | 12.8 | 13.3 | 13.9 |
| Air passenger duty | 3.6 | 3.8 | 4.0 | 4.2 | 4.4 | 4.6 | 4.8 |
| Insurance premium tax | 6.3 | 6.5 | 6.6 | 6.7 | 6.9 | 7.0 | 7.1 |
| Climate change levy | 1.9 | 2.1 | 2.2 | 2.1 | 2.3 | 2.4 | 2.6 |
| Bank levy | 2.5 | 2.4 | 1.9 | 1.1 | 1.1 | 1.1 | 1.0 |
| Bank surcharge | 1.8 | 1.5 | 1.6 | 1.6 | 1.6 | 1.7 | 1.7 |
| Apprenticeship levy | 2.6 | 2.8 | 3.0 | 3.1 | 3.2 | 3.3 | 3.5 |
| Soft drinks industry levy | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 | 0.4 |
| Digital services tax | 0.0 | 0.1 | 0.3 | 0.4 | 0.4 | 0.5 | 0.5 |
| Other HMRC taxes[4] | 7.4 | 7.4 | 7.4 | 7.6 | 7.7 | 7.7 | 7.8 |
| Vehicle excise duties | 6.5 | 6.7 | 7.1 | 7.0 | 7.2 | 7.4 | 7.6 |
| Licence fee receipts | 3.2 | 3.3 | 3.6 | 3.8 | 3.8 | 3.9 | 3.9 |
| Environmental levies | 7.5 | 10.2 | 9.6 | 9.9 | 9.8 | 10.4 | 10.8 |
| EU ETS auction receipts | 0.3 | 1.5 | 1.2 | 1.2 | 1.3 | 1.3 | 1.3 |
| Other taxes | 8.8 | 8.8 | 9.0 | 9.3 | 9.7 | 9.8 | 9.9 |
| National Accounts taxes | 735.3 | 755.8 | 786.2 | 818.2 | 853.6 | 885.0 | 918.6 |
| *Less* own resources contribution to EU | -3.4 | -3.4 | -2.4 | - | - | - | - |
| Interest and dividends | 24.0 | 27.6 | 27.6 | 28.9 | 30.6 | 32.4 | 33.9 |
| Gross operating surplus | 52.9 | 54.3 | 57.0 | 58.7 | 61.3 | 63.5 | 66.2 |
| Other receipts | 4.0 | 5.0 | 4.5 | 4.9 | 3.7 | 3.8 | 3.6 |
| Current receipts | 812.9 | 839.3 | 872.9 | 910.8 | 949.2 | 984.7 | 1,022.3 |
| *Memo: UK oil and gas revenues* [5] | *1.1* | *0.7* | *0.7* | *0.9* | *0.9* | *1.0* | *1.0* |

[1] Includes PAYE, self assessment, tax on savings income and other minor components, such as income tax repayments.
[2] National Accounts measure, gross of reduced liability tax credits.
[3] Includes SDLT, ATED and devolved property transaction taxes.
[4] Consists of landfill tax (excluding Scotland and Wales), aggregates levy, betting and gaming duties, customs duties and diverted profits tax.
[5] Consists of offshore corporation tax and petroleum revenue tax.

## Table 3.4: Changes to current receipts since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
| Income tax[1] | 0.1 | -0.5 | -0.6 | 1.5 | 2.6 | 2.2 |
| *of which:* Pay as you earn | 0.3 | 1.4 | 1.5 | 3.2 | 5.0 | 4.8 |
| Self assessment | 0.0 | -1.8 | -1.3 | -0.6 | -1.0 | -1.4 |
| Other income tax | -0.2 | -0.1 | -0.8 | -1.1 | -1.3 | -1.3 |
| National insurance contributions | -0.4 | 2.0 | 0.5 | 1.5 | 2.8 | 3.0 |
| Value added tax | 1.4 | 0.0 | -0.9 | -0.4 | 0.1 | 0.3 |
| Corporation tax[2] | 2.7 | 1.1 | 3.8 | 3.8 | 3.8 | 3.7 |
| *of which:* Onshore | 2.7 | 1.5 | 4.7 | 4.9 | 5.0 | 4.9 |
| Offshore | 0.1 | -0.4 | -0.9 | -1.1 | -1.2 | -1.3 |
| Petroleum revenue tax | 0.0 | 0.1 | 0.2 | 0.2 | 0.1 | 0.1 |
| Fuel duties | -0.2 | -0.7 | -1.7 | -2.0 | -0.6 | -0.9 |
| Business rates | -0.5 | -0.1 | -0.2 | -0.1 | -0.1 | 0.1 |
| Council tax | 0.6 | -0.1 | 0.5 | 0.5 | 0.5 | 0.5 |
| VAT refunds | 0.0 | 0.7 | 1.2 | 1.5 | 1.8 | 1.9 |
| Capital gains tax | -0.1 | 0.9 | 1.6 | 2.8 | 3.6 | 4.1 |
| Inheritance tax | 0.1 | -0.2 | 0.1 | 0.3 | 0.4 | 0.5 |
| Property transaction taxes[3] | 0.1 | 0.2 | 0.4 | 0.2 | 0.7 | 0.6 |
| Stamp taxes on shares | -0.1 | -0.3 | -0.2 | -0.2 | -0.2 | -0.2 |
| Tobacco duties | 0.0 | -0.4 | 0.0 | -0.2 | -0.2 | -0.2 |
| Alcohol duties | 0.0 | -0.5 | -1.1 | -1.1 | -1.2 | -1.2 |
| Air passenger duty | 0.1 | 0.0 | 0.1 | 0.2 | 0.2 | 0.2 |
| Insurance premium tax | 0.1 | 0.3 | 0.4 | 0.5 | 0.7 | 0.8 |
| Climate change levy | 0.0 | -0.1 | 0.0 | 0.1 | 0.2 | 0.0 |
| Bank levy | 0.0 | 0.1 | 0.1 | 0.0 | 0.0 | 0.0 |
| Bank surcharge | 0.0 | -0.4 | -0.4 | -0.4 | -0.5 | -0.5 |
| Apprenticeship levy | -0.2 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Soft drinks industry levy | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Digital services tax | 0.0 | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other HMRC taxes[4] | -0.2 | -0.2 | -0.4 | -0.4 | -0.4 | -0.4 |
| Vehicle excise duties | 0.1 | 0.2 | 0.2 | -0.1 | -0.2 | -0.3 |
| Licence fee receipts | 0.0 | -0.1 | 0.2 | 0.3 | 0.3 | 0.2 |
| Environmental levies | -0.3 | 2.0 | 0.9 | 0.7 | 0.2 | 0.5 |
| EU ETS auction receipts | -0.3 | 0.2 | -0.2 | 0.0 | -0.1 | -0.1 |
| Other taxes | 0.7 | 0.2 | 0.2 | 0.5 | 0.7 | 0.5 |
| National Accounts taxes | 3.6 | 4.6 | 4.7 | 9.8 | 15.3 | 15.3 |
| *Less* own resources contribution to EU | -0.1 | 0.0 | 1.0 | 3.5 | 3.5 | 3.5 |
| Interest and dividends | -0.5 | 0.5 | -0.3 | -0.9 | -0.9 | -0.8 |
| Gross operating surplus | 0.5 | 0.2 | 0.5 | 0.1 | 0.4 | 0.1 |
| Other receipts | -0.1 | 0.9 | 0.2 | 0.8 | 0.3 | 0.2 |
| Current receipts | 3.4 | 6.1 | 6.2 | 13.3 | 18.6 | 18.4 |
| *Memo: UK oil and gas revenues* [5] | *0.1* | *-0.3* | *-0.8* | *-0.9* | *-1.1* | *-1.2* |

[1] Includes PAYE, self assessment, tax on savings income and other minor components, such as income tax repayments.
[2] National Accounts measure, gross of reduced liability tax credits.
[3] Includes SDLT, ATED and devolved property transaction taxes.
[4] Consists of landfill tax (excluding Scotland and Wales), aggregates levy, betting and gaming duties, customs duties and diverted profits tax.
[5] Consists of offshore corporation tax and petroleum revenue tax.

## Changes in the receipts forecast since March 2019

3.26 Table 3.5 sets out the sources of changes to our receipts forecast relative to the restated March 2019 forecast we published in December. It also abstracts from the change in how we treat customs duties. On a like-for-like basis we have revised up receipts by £10.4 billion a year on average. This is more than explained by the impact of Government decisions, partly offset by a modest deterioration in our pre-measures forecast.

3.27 Government decisions have boosted receipts, both directly and indirectly, by £11.9 billion a year on average. Some of the largest impacts include:

- Cancelling the cut in the rate of corporation tax from 19 to 17 per cent due to take effect in April 2020 raises £6.4 billion a year on average from 2020-21 onwards.
- The removal of the 'red diesel' relief (a reduced fuel duty rate for non-road vehicles) increases receipts by £1.6 billion a year on average from 2022-23 onwards.
- Raising the NICs primary threshold and lower profits limit to £9,500 in 2020-21 costs £2.3 billion a year on average across the forecast.
- Higher public spending boosts receipts through two key channels. First, via the cyclical boost to the economy – which dissipates after a few years, but raises several tax bases temporarily. Second, via the temporary effect on inflation that has a persistent effect on the level of nominal GDP and thus the cash value of tax bases.
- Further rises in the National Living Wage boost the wages of affected workers, slightly offset by reduced hours worked. This boosts income tax and NICs receipts, but weighs on corporation tax receipts (through the associated profit squeeze).
- The new migration regime is expected to lower net inward migration and population growth, but with the effect concentrated among those on lower incomes. This reduces income tax and NICs receipts, as discussed in Box 3.6.

3.28 Underlying changes to our pre-measures forecast have lowered receipts by £3.0 billion a year on average from 2020-21 onwards. That follows an upward revision of £4.9 billion in 2019-20, which largely reflects one-off factors (such as a higher-than-expected special dividend from RBS). The subsequent downward revisions largely stem from the effect of weaker productivity growth on the major tax bases: lower average earnings growth weighs on income tax and NICs; lower consumer spending growth weighs on VAT receipts; and lower profit growth weighs on corporation tax. Lower interest rates materially reduce our pre-measures forecast for interest received on the government's financial assets.

## Table 3.5: Sources of change to the receipts forecast since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Restated March 2019 forecast | 833.2 | 866.7 | 897.4 | 930.6 | 966.3 | |
| *Customs duties forecast treatment change* | *-* | *0.8* | *3.2* | *3.2* | *3.3* | |
| Restated March 2019 with customs duties change | 833.2 | 867.5 | 900.6 | 933.8 | 969.5 | |
| March 2020 forecast | 839.3 | 872.9 | 910.8 | 949.2 | 984.7 | 1,022.3 |
| Like-for-like change | 6.1 | 5.4 | 10.1 | 15.4 | 15.1 | |
| | Underlying forecast changes | | | | | |
| Total | 4.9 | -1.0 | -3.5 | -4.1 | -3.5 | |
| *of which:* | | | | | | |
| Income and expenditure | 0.8 | -1.6 | -3.4 | -3.3 | -3.4 | |
| Average earnings | -0.7 | -0.7 | -1.7 | -1.8 | -2.9 | |
| Employee numbers | 1.3 | 0.6 | 0.3 | 0.8 | 1.4 | |
| Non-financial company profits | 0.1 | -0.1 | -0.4 | -0.4 | -0.3 | |
| Consumer expenditure | -0.5 | -1.6 | -1.8 | -2.0 | -1.8 | |
| Self-assessment income streams | 0.2 | 0.6 | 0.5 | 0.4 | 0.3 | |
| Other | 0.5 | -0.3 | -0.4 | -0.3 | -0.1 | |
| UK oil and gas | -0.1 | -0.8 | -0.8 | -1.1 | -1.0 | |
| Oil and gas prices | -0.3 | -1.1 | -1.1 | -1.4 | -1.3 | |
| Production and expenditure | 0.2 | 0.2 | 0.3 | 0.3 | 0.3 | |
| Property markets | 0.0 | 0.3 | 0.5 | 0.8 | 1.0 | |
| Market-derived assumptions | -0.1 | -0.6 | -1.3 | -1.8 | -2.0 | |
| Oil prices | 0.2 | 0.0 | -0.2 | -0.3 | -0.3 | |
| Equity prices | 0.1 | 0.8 | 1.1 | 1.2 | 1.3 | |
| Interest rates | -0.4 | -1.4 | -2.2 | -2.7 | -3.0 | |
| Exchange rates | 0.0 | -0.1 | 0.0 | 0.0 | 0.0 | |
| Prices | -0.2 | -0.2 | -0.2 | -0.1 | 0.0 | |
| Other economic determinants | -0.1 | 0.6 | 0.8 | 1.1 | 1.1 | |
| Other assumptions | 4.5 | 1.3 | 0.9 | 0.3 | 0.7 | |
| PAYE IT and NICs outturn and modelling | 2.3 | 1.4 | 2.3 | 3.3 | 4.6 | |
| SA IT and CGT outturn and modelling | -0.9 | -0.7 | -0.1 | -0.4 | -0.6 | |
| Onshore CT outturn and modelling | 0.5 | 0.3 | -0.5 | -0.4 | -0.5 | |
| VAT outturn and modelling | 0.0 | -0.3 | -0.4 | -0.3 | -0.2 | |
| Excise duty outturn and modelling | -1.4 | -1.8 | -2.0 | -2.2 | -2.4 | |
| Capacity markets | 1.7 | 1.1 | 0.9 | 0.5 | 0.7 | |
| Fees and fines judgements | 0.8 | 0.3 | 0.9 | 0.4 | 0.1 | |
| RBS dividends | 0.9 | 0.3 | 0.0 | 0.0 | 0.1 | |
| Other factors | 0.5 | 0.8 | -0.3 | -0.6 | -1.2 | |
| | Effect of Government decisions | | | | | |
| Total | 1.3 | 6.4 | 13.6 | 19.5 | 18.6 | 17.4 |
| *of which:* | | | | | | |
| Scorecard measures | 1.0 | 1.4 | 3.8 | 7.1 | 7.6 | 7.5 |
| Non-scorecard measures | 0.0 | 0.6 | 0.9 | 0.9 | 1.0 | 1.0 |
| Indirect effects of Government decisions | 0.3 | 4.5 | 9.0 | 11.5 | 10.0 | 8.8 |
| *of which:* | | | | | | |
| Tax and spending measures | 0.3 | 4.5 | 8.9 | 11.5 | 10.1 | 8.9 |
| Raising the National Living Wage | 0.0 | 0.0 | 0.3 | 0.7 | 1.0 | 1.4 |
| New migration regime | 0.0 | 0.0 | -0.3 | -0.7 | -1.1 | -1.5 |
| *Memo: March 2020 pre-measures forecast* | *838.0* | *866.5* | *897.1* | *929.7* | *966.0* | *1,004.9* |

## Tax-by-tax analysis

### Income tax and NICs (excluding self-assessment)

3.29 Receipts of income tax and NICs paid via the PAYE system, plus other non-SA receipts, are expected to exceed our March 2019 forecast by £3.3 billion in 2019-20. Around £3 billion of this upward revision is from higher PAYE receipts on employee salaries, thanks largely to stronger-than expected employment and earnings growth, plus higher-than-expected receipts from pension flexibility withdrawals (which continue to surprise on the upside).

3.30 With bonuses in both the financial and non-financial sectors concentrated in the final months of the financial year, receipts for 2019-20 as a whole remain uncertain. Based on the contrasting strength in receipts from these sectors in the year to date, and other indicators, we have assumed that financial sector bonuses will be flat on a year earlier, while those in the business services sector are expected to rise significantly.

3.31 The substantial rises in the personal allowance to £12,500 and the higher rate threshold to £50,000 in 2019-20 have subdued growth in PAYE income tax but boosted NICs receipts. This will reverse in 2020-21 as these thresholds are frozen in cash terms. The Budget raises the primary NICs threshold to £9,500 from April 2020, further reducing growth in NICs receipts in 2020-21. But helped by faster earnings growth in 2020, we expect growth in non-SA income tax and NICs to pick up from 3.4 per cent in 2019-20 to 4.9 per cent in 2020-21, despite the £2.1 billion cost of raising the NICs threshold.

3.32 We have revised up receipts relative to our March 2019 forecast across all years:

- Our pre-measures forecast is higher in all years and by amounts rising from 2020-21 onwards, with in-year strength and various modelling changes – for example better capturing growth in income tax on occupational pensions schemes – the main factors.

- The direct effect of Budget measures takes nearly £3 billion a year off receipts from 2020-21 onwards. This primarily reflects the more generous NICs threshold and NICs employment allowance, plus giveaways in respect of the disguised remuneration loan charge and the pensions annual allowance taper.

- The temporary boost to economic activity from the Budget package is the largest source of upward revision. In terms of real GDP, this boost is cyclical, so fades by the end of the period. But in terms of nominal GDP, and therefore wages and salaries, it persists as prices remain higher than they would otherwise have been. As a result, the effect on income tax receipts peaks in 2022-23 at £6.4 billion, but only falls back to £4.9 billion in 2024-25 despite the cyclical boost to the GDP having faded by then.

- Smaller effects come from the new migration regime, which lowers receipts by amounts rising to £1.5 billion in 2024-25, and the higher National Living Wage, which raises them by £1.4 billion by the same point.

## Table 3.6: Key changes to non-SA income tax and NICs forecasts since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| March 2019 forecast | 305.0 | 322.2 | 334.8 | 347.6 | 361.4 | |
| March 2020 forecast | 308.4 | 323.4 | 338.5 | 354.2 | 367.9 | 383.2 |
| Change | 3.3 | 1.2 | 3.7 | 6.5 | 6.5 | |
| | Underlying forecast changes | | | | | |
| Total | 3.3 | 1.5 | 1.3 | 2.8 | 3.9 | |
| *of which:* | | | | | | |
| Economic determinants | 0.6 | 0.2 | -0.4 | 0.2 | -0.1 | |
| Average earnings | -0.7 | -0.7 | -1.7 | -1.8 | -2.9 | |
| Employee numbers | 1.3 | 0.6 | 0.3 | 0.8 | 1.4 | |
| Inflation | 0.0 | 0.4 | 1.0 | 1.3 | 1.6 | |
| Other economic determinants | 0.0 | -0.2 | -0.1 | -0.1 | -0.2 | |
| Other | | | | | | |
| Recostings | 0.4 | -0.2 | 0.0 | 0.0 | -0.2 | |
| Other income tax and NICs streams | 0.4 | -0.1 | -0.5 | -0.7 | -0.6 | |
| Outturn receipts and modelling | 1.9 | 1.6 | 2.2 | 3.4 | 4.8 | |
| | Effect of Government decisions | | | | | |
| Total | 0.0 | -0.3 | 2.4 | 3.7 | 2.6 | 2.1 |
| *of which:* | | | | | | |
| Scorecard and non-scorecard measures | 0.0 | -2.9 | -2.6 | -2.7 | -2.7 | -2.8 |
| Indirect effects | 0.0 | 2.6 | 5.0 | 6.4 | 5.3 | 4.9 |

### Self-assessment (SA) income tax

3.33 Self-assessment (SA) income tax receipts in 2019-20 were £1.8 billion below our March 2019 forecast. This reflects lower 2018-19 liabilities (in part because 2017-18 liabilities were revised down in last summer's HMRC Trust Statement) and a weak initial 2019-20 payment on account (POA) in January 2020. Preliminary analysis of SA income streams showed the strongest growth was in dividend income, consistent with the effect from reducing the dividend allowance from £5,000 to £2,000.

3.34 Many taxpayers pay SA income tax through the POA mechanism. For 2019-20 liabilities, the first POA was due in January 2020, the second is due in July 2020 and the balancing payment will be made in January 2021. So cash received on liabilities for a particular year are spread across two. The weak initial POA in January 2020 means a higher level of subsequent payments in 2020-21 for a given amount of liabilities. This timing effect will boost SA receipts in 2020-21. Receipts in 2020-21 should also be buoyed by the 3.5 per cent growth in self-employment that we expect in 2019-20, given its recent strength.

3.35 Compared with March 2019, much of the weakness in SA receipts in 2019-20 pushes through the forecast. The effect from higher self-employment income relative to our March 2019 forecast is more than offset by the effect of the lower interest rates for tax on savings income (much of which is now paid through SA). The boost to the economy from the Budget package raises self-employment and, we assume, short-term interest rates relative to our pre-measures forecast. Overall, this raises SA receipts by £0.7 billion a year by 2024-25.

3.36 Budget measures raise SA receipts by around £1 billion a year by the end of the forecast. By not cutting the corporation tax rate in April 2020, the incentive to incorporate has been reduced relative to what was assumed in our pre-measures forecast (boosting SA income tax at the expense of corporation tax). And the restriction on entrepreneur's relief will mean that for those individuals who can substitute between income and capital gains, there will be a greater incentive to take earnings as income rather than capital gains.

## Table 3.7: Key changes to the SA income tax forecast since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| March 2019 forecast | 34.0 | 35.6 | 36.5 | 38.3 | 40.3 | |
| March 2020 forecast | 32.3 | 34.3 | 35.9 | 37.2 | 38.9 | 40.5 |
| Change | -1.8 | -1.3 | -0.6 | -1.0 | -1.4 | |
| | Underlying forecast changes | | | | | |
| Total | -1.8 | -1.5 | -1.6 | -2.5 | -3.0 | |
| *of which:* | | | | | | |
| Self employment income | 0.3 | 0.6 | 0.6 | 0.6 | 0.6 | |
| Dividend income | 0.0 | 0.2 | 0.0 | 0.0 | 0.0 | |
| Savings income | -0.1 | -0.3 | -0.7 | -1.0 | -1.1 | |
| Other economic determinants | -0.1 | -0.2 | -0.1 | -0.2 | -0.3 | |
| Other modelling and receipts changes | -1.9 | -1.8 | -1.4 | -1.9 | -2.2 | |
| | Effect of Government decisions | | | | | |
| Total | 0.0 | 0.2 | 1.0 | 1.5 | 1.7 | 1.6 |
| *of which:* | | | | | | |
| Scorecard and non-scorecard measures | 0.0 | 0.1 | 0.6 | 0.9 | 1.0 | 0.9 |
| Indirect effects | 0.0 | 0.1 | 0.4 | 0.6 | 0.6 | 0.7 |

### VAT

3.37 We have revised up our pre-measures forecast for VAT receipts in 2019-20 by £0.1 billion, but revised it down from 2020-21 onwards. In 2019-20, the negative effect of weaker-than-expected household spending has been offset by other factors, notably a £0.6 billion payment by HS2 (which was fiscally neutral because HS2 was compensated by central government, and has now been added to the list of entities that receive VAT refunds). From 2020-21 onwards, Table 3.8 shows the key drivers of our underlying forecast changes are:

- Weaker household spending growth in our pre-measures forecast, which in turn reflects weaker growth in productivity and real household incomes.
- A more VAT-rich composition of overall household spending provides a partial offset, as we have assumed flat rather than declining share of durables is total spending, which means a higher share of spending paying the 20 per cent standard rate.

3.38 New VAT rules allowing postponed accounting for most import VAT from January 2021 materially affect the profile of cash receipts in 2020-21 and 2021-22, but as they do not affect when the underlying VAT liability was incurred we have assumed that they will not affect accrued VAT receipts.

3.39 Downward revisions to our pre-measures forecast are partly offset by the effect of Budget policy announcements – particularly over the next couple of years:

- The direct effect of Budget measures raise VAT receipts modestly thanks to several relatively small measures that have largely offsetting effects.

- The indirect effects of Government decisions have more material effects, adding £0.7 billion a year on average, increasing until 2022-23 and then diminishing thereafter. Higher public spending adds to VAT receipts in all years, since departments pay VAT on the goods and services they procure. NLW rises add very modestly to VAT receipts via their effects on household incomes. But the tighter migration regime reduces VAT receipts by modest but rising amounts.

## Table 3.8: Key changes to the VAT forecast since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| March 2019 forecast | 136.6 | 141.5 | 146.3 | 150.9 | 155.6 | |
| March 2020 forecast | 136.6 | 140.6 | 145.9 | 151.0 | 155.8 | 160.7 |
| Change | 0.0 | -0.9 | -0.4 | 0.1 | 0.3 | |
| | Underlying forecast changes | | | | | |
| Total | 0.1 | -1.3 | -1.4 | -1.1 | -0.7 | |
| *of which:* | | | | | | |
| Household spending | -0.7 | -1.8 | -2.3 | -2.7 | -2.9 | |
| Standard rated share | 0.2 | 0.7 | 1.1 | 1.6 | 2.0 | |
| Other economic determinants | 0.6 | 0.1 | 0.1 | 0.3 | 0.5 | |
| Outturn receipts and modelling | 0.0 | -0.3 | -0.4 | -0.3 | -0.2 | |
| | Effect of Government decisions | | | | | |
| Total | -0.1 | 0.4 | 1.0 | 1.2 | 0.9 | 0.4 |
| *of which:* | | | | | | |
| Scorecard and non-scoreard measures | -0.1 | 0.0 | 0.0 | 0.1 | 0.2 | 0.1 |
| Indirect effects | 0.0 | 0.4 | 1.0 | 1.1 | 0.7 | 0.3 |
| *Memo: VAT gap (per cent)* | *7.4* | *7.4* | *7.3* | *7.3* | *7.3* | *7.3* |

3.40 The 'implied VAT gap' shown in Table 3.8 is the difference between a theoretical total and actual VAT receipts. It is adjusted for timing factors where they can be estimated. Changes in this estimate may reflect real-world changes in non-compliance or measurement errors in estimating the theoretical total. We have revised down the implied VAT gap in every year relative to our March forecast, reflecting the latest data and several modelling changes.

### Onshore corporation tax

3.41 In its September 2019 *Public sector finances* release, the ONS revised accrued corporation tax receipts down significantly, in large part due to correcting the recording of company tax credits, which had previously been double-counted. In December 2019 we restated our March 2019 onshore corporation tax forecast to be consistent with these changes.

3.42 Relative to that restated forecast we have revised receipts up by around £5 billion a year from 2020-21 onwards, which is more than explained by the effect of Budget measures. This largest yield comes from the decision not to cut the main rate from 19 to 17 per cent this April, which raises corporation tax receipts by amounts rising to £6.1 billion a year in 2024-25. Increasing the generosity of the structures and buildings allowance (by raising the main rate from 2 to 3 per cent) has a small offsetting cost. The indirect effects of policy decisions raise the tax base overall, leaving receipts higher by £0.1 billion a year.

3.43 On a pre-measures basis, we revised receipts higher in 2019-20 and 2020-21, but revised them down by an average of £0.9 billion a year thereafter. This reflects several partly offsetting factors:

- Our pre-measures forecast for cumulative profits growth is down from 2020 onwards, relative to last March. This reflects weaker productivity growth and our judgement that the profit share of national income will be squeezed in the near term. This reduces receipts by £0.4 billion a year by 2023-24. Other revisions to our economy forecast have small and offsetting effects on receipts.

- In following up the company tax credits error that was corrected in the data, we identified a related error in the estimated impact of the pre-measures cut in the main rate from 19 to 17 per cent in April 2020, which has been corrected. The costing had incorrectly been based on a measure of receipts 'net' of reduced liability tax credits. This meant that the estimated cost of the rate cut was too low. Correcting this (as well as other more minor revisions to the model) reduced our pre-measures forecast by £0.6 billion in 2023-24. This partly explains why the Budget decision to cancel this cut raises around £1 billion a year more than the Conservative manifesto suggested.

- Other modelling and data changes raise receipts in the near term, but have little effect thereafter. Cash receipts so far in 2019-20 have been stronger than expected, more than explained by strength in the life assurance sector. These firms are taxed partly on the gains on their investment holdings and so the spike in bond prices in the second half of 2019 has led to a sharp rise in receipts. Our forecast implies little change in bond prices next year, so we assume this boost to 2019-20 receipts is a one-off.

### Table 3.9: Key changes to the onshore corporation tax forecast since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| March 2019 forecast | 56.7 | 56.8 | 58.4 | 61.0 | 63.5 | |
| Corporation tax correction | -4.2 | -4.3 | -4.4 | -4.6 | -4.8 | |
| Restated March 2019 forecast | 52.5 | 52.5 | 54.0 | 56.4 | 58.7 | |
| March 2020 forecast | 54.0 | 57.2 | 58.9 | 61.4 | 63.6 | 66.0 |
| Change | 1.5 | 4.7 | 4.9 | 5.0 | 4.9 | |
| | Underlying forecast changes | | | | | |
| Total | 0.6 | 0.1 | -0.9 | -0.9 | -0.9 | |
| *of which:* | | | | | | |
| Company profits | 0.1 | -0.2 | -0.4 | -0.5 | -0.4 | |
| Other economic determinants | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| CT rate cut recosting | 0.2 | -0.3 | -0.6 | -0.6 | -0.6 | |
| Other modelling and outturn data | 0.3 | 0.6 | 0.1 | 0.2 | 0.1 | |
| | Effect of Government decisions | | | | | |
| Total | 0.9 | 4.6 | 5.8 | 6.0 | 5.8 | 5.8 |
| *of which:* | | | | | | |
| Scorecard and non-scorecard measures | 0.9 | 4.6 | 5.6 | 5.7 | 5.7 | 5.8 |
| Indirect effects | 0.0 | 0.1 | 0.2 | 0.3 | 0.1 | 0.0 |

3.44 We have revised down bank surcharge receipts by £0.4 billion a year relative to last March, a fall of around 20 per cent. This reflects particularly weak receipts during 2019, in part reflecting the weak profit performance of several banks last year. We assume that financial company profit growth will be subdued over the forecast period. In part this reflects the implications of the UK's exit from the EU, although we make no specific assumptions about the loss of passporting rights or future regulatory divergence between the UK and EU.

## Oil and gas revenues

3.45 Between 2020-21 and 2023-24, we have halved our forecast for oil and gas revenues – a downward revision of £0.9 billion a year on average. This is more than explained by much lower oil and gas prices, with our forecast conditioned on prices that are respectively 12 and 34 per cent lower in levels terms by 2023-24 than in our March 2019 forecast. Partly offsetting that, we have revised up oil production across the forecast, following stronger-than-expected production in 2018 and 2019. (Oil prices fell materially between us closing our pre-measures forecast and completing this *EFO*, reflecting concerns about how coronavirus will affect global demand. For example, dollar oil prices on 6 March were 17.8 per cent lower than the 10-day average to 11 February used in this forecast. Mechanically, that would lower our receipts forecast by £0.6 billion a year.)

## Property transaction taxes

3.46 We have revised up our forecast for property transactions taxes since March 2019 by £0.4 billion a year on average. This is primarily due to higher stamp duty land tax (SDLT) in England and Northern Ireland, but we have also revised up receipts from land and buildings transaction tax (LBTT) in Scotland and land transaction tax (LTT) in Wales. Our LBTT and LTT forecasts are detailed in our *Devolved tax and spending forecasts* publication.

3.47 The upward revisions to our SDLT forecast reflects:

- Pre-measures forecast revisions. We have revised up our pre-measures house price inflation forecast, which boosts receipts. This is partly offset by lower commercial property transactions and the small effects of other modelling changes.

- Budget measures. The introduction of a 2 per cent surcharge for non-UK residents when they buy a property in the UK is expected to raise £0.1 billion a year on average. Forestalling creates an uneven effect on receipts in 2020-21 and 2021-22.

- The indirect effect of the Budget package on house prices boosts receipts, with the effect peaking in 2021-22 and 2022-23 at £0.3 billion. This largely reflects the stronger household income growth associated with the fiscal easing.

## Table 3.10: Key changes to the property transactions tax forecasts since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| March 2019 forecast | 12.6 | 13.4 | 14.5 | 15.5 | 16.8 | |
| March 2020 forecast | 12.8 | 13.8 | 14.7 | 16.2 | 17.4 | 18.7 |
| Change | 0.2 | 0.4 | 0.2 | 0.7 | 0.6 | |
| | Underlying forecast changes | | | | | |
| Total | 0.2 | 0.1 | 0.2 | 0.3 | 0.3 | |
| *of which:* | | | | | | |
| Residential property determinants | 0.3 | 0.5 | 0.8 | 1.0 | 1.1 | |
| Commercial property determinants | -0.3 | -0.4 | -0.5 | -0.5 | -0.6 | |
| Outturn receipts and modelling | 0.1 | 0.0 | -0.1 | -0.2 | -0.3 | |
| | Effect of Government decisions | | | | | |
| Total | 0.0 | 0.3 | 0.1 | 0.4 | 0.4 | 0.2 |
| *of which:* | | | | | | |
| Scorecard and non-scorecard measures | 0.0 | 0.2 | -0.3 | 0.1 | 0.2 | 0.2 |
| Indirect effects | 0.0 | 0.1 | 0.3 | 0.3 | 0.2 | 0.1 |

### Taxes on capital

3.48 We have revised up capital gains tax receipts by £2.6 billion a year on average relative to March 2019. This reflects both a stronger pre-measures forecast and Budget measures:

- Pre-measures forecast revisions. Outturn receipts for 2018-19 were £0.9 billion higher than we expected, with liabilities paying the lower entrepreneurs' relief rate explaining almost half of that surprise (which means that the relief itself cost more than expected). We have also revised up receipts growth from 2020-21 onwards, thanks to higher equity prices and property prices, partly offset slightly by lower property transactions. (Had we conditioned our forecast on equity prices as they stood on 6 March, rather than the 10-day average to 11 February that underpins our pre-measures forecast, but holding all other aspects of our pre-measures forecast constant, CGT receipts would have been £3.2 billion lower in 2024-25.)

- Budget measures. Entrepreneur's relief has been restricted to gains of up to £1 million in a lifetime, down from £10 million. The yield from this is highly uncertain, but is estimated to £1.6 billion in 2024-25.

- The indirect effects of the Budget package further raise receipts. This reflects higher house prices due to the cyclical boost to household incomes, plus the more mechanical effect of our equity price forecast being linked to nominal GDP, which is higher.

## Table 3.11: Key changes to the capital gains tax forecast since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| March 2019 forecast | 9.1 | 9.7 | 9.9 | 10.6 | 11.6 | |
| March 2020 forecast | 10.0 | 11.4 | 12.7 | 14.3 | 15.7 | 17.0 |
| Change | 0.9 | 1.6 | 2.8 | 3.6 | 4.1 | |
| | Underlying forecast changes | | | | | |
| Total | 0.9 | 1.5 | 1.9 | 2.1 | 2.4 | |
| *of which:* | | | | | | |
| Equity prices | 0.0 | 0.6 | 0.9 | 1.0 | 1.1 | |
| House prices and transactions | 0.0 | 0.1 | 0.1 | 0.2 | 0.2 | |
| Outturn receipts and other modelling | 0.9 | 0.7 | 0.9 | 1.0 | 1.1 | |
| | Effect of Government decisions | | | | | |
| Total | 0.0 | 0.2 | 0.9 | 1.5 | 1.7 | 1.7 |
| *of which:* | | | | | | |
| Scorecard and non-scorecard measures | 0.0 | 0.2 | 0.8 | 1.2 | 1.4 | 1.5 |
| Indirect effects | 0.0 | 0.0 | 0.1 | 0.3 | 0.3 | 0.2 |

3.49 We have revised up inheritance tax receipts by £0.2 billion a year on average. This largely reflects higher mortality assumptions, plus higher equity and house prices. This is partly offset by the effect of new outturn data.

3.50 We have revised down stamp duty on shares by £0.2 billion a year on average, due to weaker-than-expected receipts in 2019-20 partly offset by higher equity prices.

### Excise duties

3.51 Fuel duties have been revised down by £1.2 billion a year on average. This reflects:

- A lower pre-measures forecast, thanks to a £0.7 billion downward revision to 2019-20 receipts that persists over the forecast, a small reduction due to lower RPI inflation, and a £0.8 billion reduction as a result of faster improvements in fuel efficiency than we assumed last March (part of which reflects new emission fines discussed in Box 3.1).

- Budget measures include the now familiar one-year freeze in the main rate of fuel duty, which reduces receipts by £0.5 to £0.6 billion a year from 2020-21 onwards. But this is more than offset by restricting eligibility to use 'red diesel', which raises £1.8 billion a year from 2022-23 onwards by requiring more fuel users to pay the higher main rate.

3.52 We have revised down alcohol duties by £1.0 billion a year on average. This mostly reflects lower-than-expected receipts so far this year, which we assume will persist over the forecast. Lower RPI inflation and consumer expenditure also lower receipts, while the latest alcohol duty freeze announced in this Budget costs £0.3 billion a year on average.

3.53 We have revised tobacco duties down by £0.2 billion a year on average relative to our March forecast. We have revised down receipts in 2019-20 by £0.4 billion due to lower-than-expected clearances. We think part of the shortfall in 2019-20 is due to uncertainty about the timing of duty uprating generated by the cancelled Autumn Budget, so we have assumed only half the shortfall will persist over the forecast.

3.54 The early General Election meant that the existing RPI duty uprating did not go ahead and the 2 per cent duty escalator expired (as it was only in place until the end of the Parliament). The RPI duty uprating is now set to take place on Budget day and the 2 per cent escalator has been reinstated for this Parliament.

## Business rates

3.55 Business rates are calculated by multiplying the rateable value of non-domestic property by the 'multiplier', which is uprated with CPI inflation, minus any reliefs. The main change since our March 2019 forecast is the Budget announcement that the retail discount for properties with a rateable value under £51,000 will be increased from 33 to 50 per cent for 2020-21. Raising the generosity of the retail discount costs £250 million in 2020-21, bringing the full cost of the discount to around £750 million. With no announced policy thereafter, we assume there is no retail discount from 2021-22 onwards.

3.56 On a pre-measures basis, business rates are little changed from March 2019. Lower CPI inflation pushes down the multiplier reducing receipts by around £0.3 billion a year by 2023-24. This is offset by provisional information from local authorities on expected yield in 2020-21, adding around £0.5 billion a year to receipts from 2020-21 onwards.

## Other taxes

3.57 Vehicle excise duty (VED) receipts are expected to be higher over the first half of the forecast, mostly due to stronger-than-expected receipts in 2019-20 that we assume will persist. From 2021-22 onwards we have revised receipts down due to modelling changes in our new car sales forecast and faster improvements in new car efficiency thanks to new $CO_2$ emissions targets and associated fines that are described in Box 3.1.

3.58 We have revised up VAT refunds by £1.4 billion a year on average. This is mostly driven by higher government procurement and investment reflecting the large rise in public spending announced in the Budget. Adding HS2 to the entities that can claim VAT refunds has added £0.3 billion a year on average to the forecast.

3.59 We have revised up insurance premium tax (IPT) by £0.5 billion on average since March 2019. Receipts so far this year have been unexpectedly strong and so we have revised up our growth assumption over the forecast as well as assuming a higher starting point.

3.60 The UK-issued allowances under the EU emissions trading scheme (EU ETS) restarted on 4 March 2020, following the ratification of the Withdrawal Agreement.[9] The total allowances included in the auction calendar amount to the combined volumes to be auctioned by the UK for the calendar years 2019 and 2020. Changes in receipts mostly reflect the new published auction schedule. We have assumed that this spike in cash receipts is spread out over 2019 and 2020, approximating the ONS accruals treatment in the public finances.

3.61 During the transition period the UK continues to have access to EU ETS, but the status of the UK's membership thereafter remains uncertain. The Treasury told us that "*the UK will implement a system of carbon pricing of at least the same effectiveness and scope as the EU Emissions Trading System (EU ETS). A consultation by the UK Government and the devolved administrations sets out the preferred option to establish a UK ETS and link it to the EU ETS or, if this cannot be achieved, implement a standalone UK ETS or a Carbon Emissions Tax.*"

3.62 In the absence of further policy detail this forecast has been prepared as though the UK remained a member of the EU ETS, that allowances beyond 2021 will broadly match the pre-Brexit planned auction schedule, and that receipts will reflect current futures prices for carbon allowances. We will revisit this in the autumn in the light of any firmer policy.

3.63 BBC licence fee receipts have been revised up by £0.2 billion a year on average. This is more than accounted for by the BBC's decision to means-test free TV licences for those over the age of 75 by limiting them to people in receipt of pension credit. We discussed this in Box 5.1 of our 2019 *Fiscal risks report*. The induced rise in spending on pension credit is included in our welfare spending forecast. We assume the BBC spends the higher receipts.

3.64 Our forecast for council tax is up by £0.4 billion a year on average over the forecast period, reflecting the Government's decision to increase the amount by which local authorities can increase council tax rates without a referendum. Our forecast for local authority income and spending is set out in the spending section below.

3.65 Customs duties comprise the majority of 'traditional own resources' or TOR-based contributions to the EU until the end of the transition period in December 2020. Until now our post-referendum forecasts have continued to treat them as though they are collected on behalf of the EU – equivalent in fiscal terms to assuming they are spent once they become UK receipts and consistent with our approach to the EU contributions in our spending forecast. We have switched to presenting them on a gross basis in this forecast. As the Government is consulting on its new post-Brexit tariff schedule, we have not incorporated any proposed changes in this forecast, and have assumed that the present schedule persists beyond January 2021. Once sufficient detail about the new schedule is available, we will incorporate it into our forecast and show what it costs or yields relative to the present system. We have revised down customs duties receipts by £0.2 billion a year on average.

[9] ICE, Emissions Auction 2020 Calendar.

3.66 Environmental levies include levy-funded spending policies such as the renewables obligation (RO), contracts for difference (CfD) and the capacity markets scheme. We also include receipts from the 'CRC energy efficiency scheme' until its abolition after the 2018-19 compliance year (with final receipts scored in 2019-20). The Budget announcement of a green gas levy boosts environmental levies by £95 million in 2024-25.

3.67 The capacity markets scheme (which focuses on the security of electricity supply) has resumed following the lifting of the suspension of the scheme in October 2019. It had been suspended following a European Court of Justice ruling that removed its state aid approval. Given the uncertainty over the timing of the resumption, our March 2019 forecast had set post-suspension capacity markets tax and spend to zero. The £1.7 billion from the capacity markets scheme in 2019-20 mainly reflects deferred payments from the suspension period. Thereafter, the tax and spend from the scheme reflects auctions held to date and an assumption that future auctions will clear at an average of historical clearing prices. Given its treatment in the public finances, this scheme is neutral for borrowing.

### Other receipts

3.68 We have revised up fines and penalties from the Serious Fraud Office (SFO), Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) in 2019-20 by £0.8 billion, thanks to the €1.0 billion SFO fine paid by Airbus SE. We have assumed that fines of this size will not be repeated in future years, so our forecast reverts to levels more consistent with those recorded in recent years prior to 2019-20. In future years, we have incorporated an estimate of new car emissions fines (discussed in Box 3.1).

### Box 3.1: New car emission fines

In April 2019, the European Parliament and Council adopted new regulations to set mandatory emissions targets for new cars. These targets are being phased in from 2020 and apply in full from 2021. They set an EU-wide fleet emissions target of 95 grams of $CO_2$ per kilometre for new cars. In broad terms, each manufacturer faces a fine of €95 per new car registered for each gram deviation above this target (on a fleet-wide average basis). Each manufacturer will face a separate weight-adjusted target and 'super credits' will be issued between 2020 and 2022 for zero and very low emission cars.

We asked the Government whether it will continue to levy these fines from 1 January 2021, after the Brexit transition period ends, as this would represent a new source of income for the Exchequer. It told us that "*all of the provisions of the $CO_2$ regulatory regime as it stands, including those relating to the targets and fines for non-compliance*" transferred into UK law on 31 January 2020 under the terms of the EU Withdrawal Act. It also told us that the Government has committed to "*pursue a future approach that is at least as ambitious as the current arrangements for vehicle emissions regulation*" via its 'Road to Zero' strategy.[a] We therefore need to forecast the effect of these fines on the public finances.

The latest Society of Motor Manufacturers and Traders (SMMT) data the average emissions of new cars in the UK in 2019 was 127.9 grams of $CO_2$ per kilometre, around 35 per cent above

the current EU-wide 2021 target.[b] On that basis, hitting that target in 2021 would require falls of around 14 per cent a year in 2020 and 2021 – versus an average over the past ten years of just 2 per cent a year (according to the SMMT). Some policy details have yet to be finalised, for example with respect to 'pooling' (whereby manufacturers can group together to meet emissions targets jointly) and any exemptions for smaller manufacturers (which form part of the current EU regime). We have drawn on a range of external estimates of the new regime's effect at the EU level to generate our own UK forecast for the fines. We also adjust our forecasts for fuel duty and vehicle excise duties (VED) to be consistent with the path for new car efficiencies that results.

Several external studies have estimated the firm-level impact of these fines at an EU level, with totals varying widely from €2 billion to €34 billion (with some studies looking at 2020 and others at 2021).[c,d,e] Given the scale of the fines, we have assumed that the average emission rating of new cars in the UK will hit the target only two years late, in 2023, despite the marked change required relative to the trend of the past ten years. This implies an average fall in measured emissions of around 7 per cent a year. This generates a central estimate that these fines will raise £0.9 billion in 2021-22 and diminishing amounts thereafter as car manufacturers meet their targets. In the absence of further policy detail, we assume that the fines will accrue at the point the emissions are reported. As Table A shows, this yield is more than offset by the indirect cost of faster improvements in fuel efficiency reducing fuel duty and VED receipts.

Given the approach we have needed to take to estimate the fines revenue, there is clearly significant uncertainty around these figures. If manufacturers were able to hit the target in 2021, it would reduce overall receipts by around £1.5 billion in 2021-22, relative to our current forecast (reflecting both lower fines revenue and lower fuel duty and VED receipts).

## Table A: Impact of new car emission fines

| | £ billion | | | | |
|---|---|---|---|---|---|
| | Forecast | | | | |
| | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| New car emissions fines | 0.3 | 0.9 | 0.4 | 0.1 | 0.0 |
| Effect on fuel duty | -0.1 | -0.2 | -0.3 | -0.4 | -0.5 |
| Effect on vehicle excise duties | -0.1 | -0.2 | -0.3 | -0.2 | -0.2 |
| Total effect on receipts | 0.1 | 0.5 | -0.2 | -0.6 | -0.7 |

[a] *The Road to Zero: Next steps towards cleaner road transport and delivering our Industrial Strategy*, HM Government, July 2018.
[b] *SMMT New Car Registrations*, SMMT, January 2020.
[c] *Automakers sprint for electrification as large fines loom for emissions*, Moody's Investor Service, April 2019.
[d] *CO2 emissions are increasing. Car makers must act, PA Consulting, January 2020.*
*e 2021 CO2 targets would generate €34 billion euros in penalty payments within Europe, JATO Dynamics, April 2019.*

3.69 Interest and dividend receipts include income from the government's financial assets, among them student loans and bank deposits held by the Debt Management Office and local authorities. It also includes dividends from the Government's shareholding in RBS. Our March 2019 restated forecast incorporated the change in the scoring of accrued interest on student loans and the inclusion of income from funded public sector pension schemes.

3.70 Relative to that March forecast, interest and dividend receipts are up £0.5 billion in 2019-20, but down by around £0.9 billion a year from 2021-22 onwards. This reflects:

- Higher-than-expected special dividends from RBS in 2019-20, with the Government receiving £1.8 billion of dividends – around twice what we assumed last March. The forecast for future years has been updated for the new profile of RBS share sales. RBS dividends drop back over the forecast period reflecting the sales and that we do not assume additional special dividend payouts in the future.

- Lower interest rates (despite our use of a higher path than assumed by financial markets) take around £1.1 billion a year off receipts by 2023-24.

3.71 Accrued interest on student loans is down by an average of £0.1 billion a year. Lower inflation and interest rates reduce accrued interest, but the cancellation of student loans asset sales means interest on those loans will no longer be foregone.

3.72 We have revised our public sector gross operating surplus (GOS) forecast up by an average of £0.3 billion a year from 2019-20 onwards. This is driven by increases to our forecast for borrowing-financed spending by local authorities, some of which is delivered through their housing revenue accounts (HRAs). This increases GOS by £1.1 billion a year by 2023-24, but is neutral for borrowing, as it also reduces expenditure by the same amount as an accounting adjustment. Partially offsetting this is a downward revision to Transport for London (TfL) operating revenues, which we have drawn from the latest TfL business plan, and reduce GOS by £0.8 billion by the end of the forecast period.

## Public sector expenditure

### Definitions and approach

3.73 This section explains our forecast for public sector expenditure, which is based on the National Accounts aggregates for public sector current expenditure (PSCE), public sector gross investment (PSGI) and total managed expenditure (TME) – the sum of PSCE and PSGI. In our forecast, we combine these National Accounts aggregates with the two administrative aggregates used by the Treasury to manage public spending:

- Departmental expenditure limits (DELs)[10] currently account for just under half of spending – mostly covering spending on public services, grants and administration ('resource' spending), and investment ('capital' spending). These are items that can be planned over extended periods. Our fiscal forecast therefore shows PSCE in resource DEL and PSGI in capital DEL. We typically assume (in line with past experience) that departments will underspend the final limits that the Treasury sets for them, so – unless otherwise stated – when we refer to PSCE in RDEL and PSGI in CDEL (or RDEL and CDEL for simplicity) we mean the net amount that we assume will actually be spent.

[10] Our presentation of expenditure only shows those components of RDEL, CDEL and AME that are included in the fiscal aggregates of PSCE and PSGI. For budgeting purposes, the Treasury also includes other components in DEL and AME such as non-cash items and financial transactions, which are discussed later in this chapter.

- Annually managed expenditure (AME) accounts for just over half of spending – items less amenable to multi-year planning, such as social security and debt interest. Again, our fiscal forecast shows PSCE in current AME and PSGI in capital AME.

## Summary of the expenditure forecast

3.74 Table 3.12 summarises our latest forecast for public spending. TME is expected to rise by 1.4 per cent of GDP between 2018-19 and 2024-25, as higher resource and capital departmental spending (which rise by 1.8 and 1.2 per cent of GDP respectively) is only part offset by lower AME spending (which falls by 1.6 per cent of GDP). The largest fall is the 0.6 per cent of GDP drop in the net cost of public service pensions, while debt interest, welfare spending and local authority capital spending also fall as a share of GDP.

### Table 3.12: TME split between DEL and AME

| | Per cent of GDP | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| TME | 39.3 | 39.8 | 40.3 | 40.8 | 40.8 | 40.8 | 40.7 |
| *of which:* | | | | | | | |
| TME in DEL | 16.0 | 16.9 | 17.8 | 18.5 | 18.7 | 18.9 | 19.0 |
| *of which:* | | | | | | | |
| PSCE in RDEL | 13.6 | 14.2 | 14.7 | 15.1 | 15.2 | 15.3 | 15.4 |
| PSGI in CDEL | 2.3 | 2.7 | 3.1 | 3.4 | 3.5 | 3.6 | 3.6 |
| TME in AME | 23.3 | 22.9 | 22.4 | 22.3 | 22.1 | 21.9 | 21.7 |
| *of which:* | | | | | | | |
| Welfare spending | 10.3 | 10.1 | 10.0 | 9.9 | 10.0 | 10.0 | 10.1 |
| Debt interest, net of APF | 1.7 | 1.7 | 1.5 | 1.6 | 1.5 | 1.5 | 1.4 |
| Locally financed current expenditure | 2.4 | 2.4 | 2.4 | 2.3 | 2.3 | 2.3 | 2.3 |
| Net public service pension payments | 0.6 | 0.3 | 0.2 | 0.1 | 0.1 | 0.0 | 0.0 |
| Other PSCE in AME | 6.3 | 6.6 | 6.6 | 6.6 | 6.5 | 6.4 | 6.3 |
| PSGI in AME | 1.9 | 1.8 | 1.8 | 1.7 | 1.7 | 1.7 | 1.7 |

3.75 Tables 3.13 and 3.14 detail our latest spending forecast and the changes since last March. For the first time, public spending exceeds £1 trillion a year – from 2022-23 onwards.

## Table 3.13: Total managed expenditure

| | £ billion | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Public sector current expenditure (PSCE) | | | | | | | |
| PSCE in RDEL | 295.6 | 316.3 | 339.8 | 361.3 | 375.9 | 391.8 | 408.6 |
| PSCE in AME | 462.7 | 471.4 | 476.0 | 492.8 | 505.6 | 518.1 | 532.2 |
| *of which:* | | | | | | | |
| Welfare spending | 222.8 | 224.6 | 231.2 | 237.8 | 246.8 | 256.9 | 266.8 |
| *of which:* | | | | | | | |
| Inside welfare cap | 119.5 | 119.0 | 122.6 | 124.3 | 127.0 | 130.2 | 133.5 |
| Outside welfare cap | 103.3 | 105.6 | 108.6 | 113.5 | 119.8 | 126.7 | 133.4 |
| Locally financed current expenditure | 52.7 | 53.9 | 55.0 | 55.1 | 56.9 | 58.6 | 60.1 |
| Central government debt interest, net of APF[1] | 37.5 | 38.2 | 34.5 | 37.8 | 37.9 | 37.3 | 36.8 |
| Scottish Government's current expenditure | 27.9 | 32.0 | 33.5 | 35.6 | 37.4 | 38.9 | 40.7 |
| Expenditure transfers to EU institutions[2] | 12.2 | 11.0 | 9.0 | 11.1 | 8.4 | 4.7 | 2.2 |
| Assumed spending in lieu of EU transfers[2] | - | - | - | - | - | - | - |
| Net public service pension payments | 12.9 | 6.9 | 4.2 | 2.9 | 2.0 | 1.2 | 0.3 |
| Company and other tax credits | 6.2 | 6.8 | 7.4 | 7.9 | 8.4 | 8.8 | 9.2 |
| BBC current expenditure | 3.0 | 3.8 | 4.0 | 4.0 | 4.1 | 4.1 | 4.2 |
| National lottery current grants | 1.2 | 1.3 | 1.3 | 1.1 | 1.0 | 1.0 | 0.9 |
| General government imputed pensions | 0.9 | 1.3 | 1.3 | 1.3 | 1.3 | 1.3 | 1.3 |
| Public corporations' debt interest | 0.4 | 0.4 | 0.4 | 0.4 | 0.5 | 0.5 | 0.5 |
| Funded public sector pension schemes | 18.7 | 19.5 | 20.5 | 21.4 | 22.4 | 23.5 | 24.6 |
| General government depreciation | 41.1 | 42.2 | 44.1 | 45.7 | 47.4 | 49.3 | 51.3 |
| Current VAT refunds | 16.1 | 16.9 | 17.7 | 18.4 | 19.1 | 19.7 | 20.9 |
| Environmental levies | 7.8 | 10.7 | 10.6 | 11.0 | 10.9 | 11.5 | 12.0 |
| Other PSCE items in departmental AME[3] | 2.2 | 1.6 | 1.2 | 1.4 | 1.5 | 1.5 | 1.6 |
| Other National Accounts adjustments | -1.0 | 0.3 | 0.1 | -0.2 | -0.5 | -0.8 | -1.2 |
| Total public sector current expenditure | 758.3 | 787.7 | 815.8 | 854.1 | 881.5 | 909.9 | 940.8 |
| Public sector gross investment (PSGI) | | | | | | | |
| PSGI in CDEL | 50.8 | 59.9 | 71.2 | 82.2 | 86.6 | 91.5 | 94.8 |
| PSGI in AME | 42.2 | 39.1 | 40.7 | 41.1 | 42.6 | 43.5 | 44.6 |
| *of which:* | | | | | | | |
| Locally financed capital expenditure | 13.1 | 13.1 | 10.9 | 10.3 | 10.8 | 10.3 | 10.4 |
| Public corporations' capital expenditure | 9.9 | 11.0 | 11.4 | 11.4 | 11.5 | 11.7 | 11.9 |
| Student loans | 10.1 | 9.8 | 10.6 | 11.2 | 11.9 | 12.4 | 12.8 |
| Funded public sector pension schemes | 1.6 | 0.8 | 0.9 | 0.9 | 0.9 | 0.9 | 0.9 |
| Scottish Government's capital expenditure | 3.4 | 4.0 | 4.6 | 5.4 | 5.6 | 5.8 | 6.0 |
| Tax litigation | 0.0 | 0.0 | 1.8 | 1.2 | 1.1 | 1.1 | 1.1 |
| Other PSGI items in departmental AME[3] | 6.8 | 0.8 | 0.8 | 0.8 | 0.8 | 0.7 | 0.6 |
| Other National Accounts adjustments | -2.7 | -0.4 | -0.3 | 0.0 | 0.0 | 0.6 | 0.7 |
| Total public sector gross investment | 93.0 | 99.1 | 111.9 | 123.3 | 129.2 | 135.0 | 139.4 |
| *Less* public sector depreciation | -48.8 | -49.9 | -52.2 | -54.0 | -56.0 | -58.1 | -60.3 |
| Public sector net investment | 44.3 | 49.1 | 59.7 | 69.3 | 73.2 | 77.0 | 79.1 |
| Total managed expenditure | 851.3 | 886.8 | 927.7 | 977.4 | 1,010.7 | 1,044.9 | 1,080.2 |

[1] Includes reductions in debt interest payments due to the APF.
[2] From 2019-20 onwards, the expenditure transfers to EU institutions reflect the estimated cost of the financial settlement that the UK will pay the EU after Brexit.
[3] Includes Network Rail current and capital expenditure in 2018-19 only.

## Table 3.14: Changes to total managed expenditure since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
| Public sector current expenditure (PSCE) | | | | | | |
| PSCE in RDEL | 1.5 | 4.1 | 15.2 | 27.0 | 31.2 | 34.9 |
| PSCE in AME | 1.3 | 2.7 | -1.2 | -1.2 | -6.3 | -12.8 |
| *of which:* | | | | | | |
| Welfare spending | -0.2 | -2.7 | -1.0 | -2.2 | -2.7 | -3.6 |
| *of which:* | | | | | | |
| Inside welfare cap | 0.2 | -2.4 | -0.6 | -1.7 | -2.5 | -3.5 |
| Outside welfare cap | -0.4 | -0.3 | -0.4 | -0.5 | -0.2 | -0.1 |
| Locally financed current expenditure | 0.9 | -0.4 | 1.9 | -0.1 | 0.0 | 0.0 |
| Central government debt interest, net of APF[1] | 0.5 | -2.0 | -4.4 | -2.5 | -3.7 | -5.0 |
| Scottish Government's current expenditure | 0.3 | 4.0 | 3.8 | 4.9 | 5.7 | 5.9 |
| Expenditure transfers to EU institutions[2] | -0.1 | -1.7 | -1.5 | 0.7 | 0.7 | 0.6 |
| Assumed spending in lieu of EU transfers[2] | - | - | -3.0 | -3.0 | -5.6 | -9.3 |
| Net public service pension payments | 0.3 | 0.2 | -2.2 | -4.3 | -5.9 | -7.0 |
| Company and other tax credits | 1.1 | 1.6 | 2.2 | 2.7 | 3.0 | 3.2 |
| BBC current expenditure | -0.9 | 0.0 | 0.2 | 0.3 | 0.3 | 0.2 |
| National lottery current grants | 0.0 | -0.1 | 0.1 | -0.1 | -0.2 | -0.2 |
| General government imputed pensions | -0.4 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Public corporations' debt interest | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Funded public sector pension schemes | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| General government depreciation | 0.1 | -0.1 | 0.1 | -0.2 | -0.3 | -0.4 |
| Current VAT refunds | 0.1 | 0.7 | 0.8 | 1.1 | 1.2 | 1.3 |
| Environmental levies | -0.3 | 2.0 | 0.9 | 0.6 | 0.2 | 0.5 |
| Other PSCE items in departmental AME[3] | 0.4 | 0.4 | 0.1 | 0.1 | 0.1 | 0.1 |
| Other National Accounts adjustments | -0.3 | 0.8 | 0.8 | 0.8 | 0.8 | 0.9 |
| Total public sector current expenditure | 2.8 | 6.8 | 14.0 | 25.8 | 25.0 | 22.1 |
| Public sector gross investment (PSGI) | | | | | | |
| PSGI in CDEL | -0.4 | -0.4 | 5.7 | 13.4 | 15.4 | 16.1 |
| PSGI in AME | -1.6 | -0.5 | 1.1 | 3.1 | 4.2 | 7.1 |
| *of which:* | | | | | | |
| Locally financed capital expenditure | -1.0 | 0.8 | 0.8 | 0.5 | 1.3 | 1.4 |
| Public corporations' capital expenditure | 0.3 | 1.4 | 1.7 | 1.8 | 1.9 | 1.9 |
| Student loans | 0.0 | -1.4 | -1.0 | -0.7 | -0.3 | 2.0 |
| Funded public sector pension schemes | 0.0 | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 |
| Scottish Government's capital expenditure | 0.0 | -0.2 | 0.1 | 0.5 | 0.6 | 0.7 |
| Tax litigation | 0.0 | -1.3 | -0.6 | 0.8 | 0.7 | 0.7 |
| Other PSGI items in departmental AME[3] | 0.8 | 0.2 | -0.1 | -0.1 | -0.1 | -0.1 |
| Other National Accounts adjustments | -1.7 | 0.1 | 0.1 | 0.3 | 0.2 | 0.5 |
| Total public sector gross investment | -2.0 | -0.9 | 6.8 | 16.6 | 19.7 | 23.2 |
| *Less* public sector depreciation | -0.1 | -0.1 | -0.6 | -0.5 | -0.6 | -0.6 |
| Public sector net investment | -2.1 | -1.0 | 6.2 | 16.1 | 19.1 | 22.6 |
| Total managed expenditure | 0.8 | 6.0 | 20.8 | 42.4 | 44.7 | 45.3 |

[1] Includes reductions in debt interest payments due to the APF.
[2] From 2019-20 onwards, the expenditure transfers to EU institutions reflect the estimated cost of the financial settlement that the UK will pay the EU after Brexit.
[3] Includes Network Rail current and capital expenditure in 2018-19 only.

3.76 Table 3.15 summarises the sources of changes to our forecast since March 2019. It compares our latest forecast to a restated March 2019 baseline that has also been adjusted for the change in how we present customs duties and the assumed post-Brexit spending associated with it in our pre-measures forecast. On that basis, it shows that we have revised spending up by progressively larger amounts, reaching £42.1 billion in 2023-24.

3.77 Government policy decisions explain the vast majority of the upward revision:

- Departmental spending envelopes have been set for this year's Spending Review at levels far higher than those assumed in our March 2019 forecast. Even after assumed underspending relative to those higher totals, this raises RDEL and CDEL spending in 2024-25 by £38.9 billion and £16.7 billion respectively. The knock-on effects of these rises to Scottish Government AME spending are £3.9 billion and £1.8 billion.
- These large increases in DEL spending mean that we can now remove our post-referendum forecast assumption that direct Brexit fiscal savings would be spent on other domestic priorities, since that has now come to pass. In effect, this finances part of the higher DEL spending, by amounts rising to £14.6 billion in 2024-25 (Box 3.5).
- Other spending measures include raising the R&D tax credit main rate from 12 to 13 per cent, which raises current spending, and cancelling planned student loan sales, which removes the capital spending associated with selling them at a discount.
- Higher RDEL spending boosts public service pension scheme income via higher contributions. As more than 10 per cent of RDEL goes on pension contributions, this reduces the net cost of the schemes by amounts rising to £4.3 billion in 2024-25.
- Other indirect effects of the Budget package include the higher debt interest spending associated with higher borrowing, higher RPI inflation and higher interest rates.
- Raising the National Living Wage has a largely neutral effect on welfare.
- The new migration regime reduces welfare spending because the associated decline in migrants from the EU is concentrated among those in the income bracket that is most likely to be eligible for means-tested in-work support.

3.78 Our pre-measures forecast revisions are small by comparison. Lower interest rates and lower inflation have reduced spending materially, particularly on debt interest. The combined effect of these changes reduces spending by £8.8 billion in 2023-24. Partly offsetting that, we have revised up growth in spending on incapacity benefits, which largely explains the upward revision to welfare spending. We have also revised up the expected cost of R&D tax credits in our pre-measures forecast, reflecting higher outturns, and borrowing-financed capital spending by local authorities, reflecting recent trends.

## Table 3.15: Sources of change to the spending forecast since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Restated March 2019 forecast | 880.8 | 906.9 | 935.0 | 966.0 | 999.6 | |
| *Customs duties forecast treatment change* | 0.0 | 0.8 | 3.2 | 3.2 | 3.3 | |
| Restated March 2019 with customs duties change | 880.8 | 907.7 | 938.2 | 969.3 | 1,002.8 | |
| March 2020 forecast | 886.8 | 927.7 | 977.4 | 1,010.7 | 1,044.9 | 1,080.2 |
| Like-for-like change | 6.0 | 20.0 | 39.2 | 41.4 | 42.1 | |
| | Underlying forecast changes | | | | | |
| Total forecast changes | 5.3 | 1.2 | 1.6 | -0.6 | -2.0 | |
| *of which:* | | | | | | |
| Economic determinants | -2.1 | -4.1 | -3.6 | -3.6 | -3.7 | |
| Inflation changes | -1.9 | -4.1 | -3.4 | -3.4 | -3.3 | |
| Other | -0.2 | 0.0 | -0.2 | -0.2 | -0.3 | |
| Market assumptions: interest rates | -0.2 | -2.2 | -3.2 | -4.3 | -5.2 | |
| Other assumptions and changes | 7.6 | 7.5 | 8.3 | 7.4 | 6.9 | |
| DEL forecast changes | 1.3 | 0.0 | - | - | - | |
| Other changes to the welfare forecast | 0.2 | 2.8 | 3.0 | 2.9 | 2.5 | |
| Scottish government expenditure | 1.0 | -0.4 | -0.8 | -0.8 | -1.0 | |
| Net expenditure transfers to EU institutions | -1.7 | -0.9 | -0.4 | -0.8 | -0.5 | |
| Net public service pension payments | 0.2 | -0.4 | -1.0 | -2.0 | -2.7 | |
| Locally financed capital expenditure and public corporations' capital expenditure | 2.3 | 2.3 | 2.5 | 3.3 | 3.4 | |
| Other changes to central government debt interest, net of APF | 0.2 | -1.1 | -1.7 | -1.8 | -1.9 | |
| Company and other tax credits | 1.6 | 2.2 | 2.5 | 2.6 | 2.8 | |
| Student loans | 0.7 | 1.3 | 1.9 | 2.4 | 2.5 | |
| Environmental levies | 2.0 | 0.9 | 0.6 | 0.2 | 0.5 | |
| Other | -0.3 | 0.7 | 1.7 | 1.3 | 1.1 | |
| | Effect of Government decisions | | | | | |
| Total effect of Government decisions | 0.7 | 18.7 | 37.6 | 42.0 | 44.0 | 46.5 |
| *of which:* | | | | | | |
| Higher departmental spending | 2.5 | 20.9 | 40.5 | 46.7 | 51.1 | 55.5 |
| Use of direct Brexit fiscal savings | 0.0 | -4.3 | -5.0 | -7.1 | -11.3 | -14.6 |
| Other spending measures | -2.1 | 1.1 | 0.3 | 0.7 | 2.6 | 3.9 |
| DEL effect on public service pensions | 0.0 | -1.7 | -3.0 | -3.5 | -4.0 | -4.3 |
| Raising the National Living Wage | 0.0 | 0.0 | -0.1 | -0.1 | -0.1 | 0.0 |
| New migration regime | 0.0 | 0.0 | 0.0 | -0.1 | -0.3 | -0.5 |
| Other budget package indirect effects | 0.3 | 2.8 | 5.0 | 5.5 | 6.0 | 6.4 |

## Spending within departmental expenditure limits

### DEL spending and changes since March 2019

3.79 In this section, we use 'RDEL spending' and 'CDEL spending' to refer to PSCE in RDEL and PSGI in CDEL. Our forecasts reflect:

- Departments' latest 'forecast outturns' for 2019-20 that were sent to the Treasury in February, the local government finance settlement and this year's Supplementary Estimates, plus our assumptions regarding any further underspending relative to them.
- Departments' plans for 2020-21 as announced in the 2019 Spending Round plus the further additions announced in this Budget, including our assumptions regarding likely underspending against these latest plans.
- The Government's Budget announcements on the total DEL envelopes for 2021-22 to 2023-24 that will be allocated at the Spending Review later this year. These are significantly higher than the provisional totals on which our March 2019 forecast was based. Although some DELs have already been allocated to departments, most will not be finalised until the Spending Review. DELs already allocated include the NHS RDEL settlement to 2023-24 and the schools RDEL settlement to 2022-23.
- The Government's latest provisional total DELs for 2024-25.

3.80 Table 3.16 shows our forecasts for RDEL and CDEL spending and overall changes relative to our March forecast; these changes are broken down in Table 3.17. We present plans, underspends and actual spending in every year. For years covered by actual plans or the envelope for this year's Spending Review, our forecasts for actual spending are generated by subtracting underspends from the totals that have been set. For 2024-25, the Treasury has stated how much it intends to spend in total and we show the implied plans and underspends that we think would be consistent with that level of actual spending.

3.81 Table 3.16 shows that:

- Actual resource spending has been revised up in 2019-20, as a result of the additional funding announced in the Spending Round together with our expectation that departments will underspend those new plans by less than we assumed last year. In 2020-21 actual spending is up £15.2 billion, thanks largely to increases announced in the 2019 Spending Round plus some further additions in the Budget. The Budget has set limits for the Spending Review years that are even higher, increasing spending by amounts rising to £34.9 billion in 2023-24 after allowance for underspends.
- Actual capital spending is little changed in 2019-20 but £5.7 billion higher in 2020-21, reflecting the increase announced in the Spending Round and this Budget (partially offset by a slightly higher underspend than we assumed last year). The Budget has set totals for the Spending Review years that are much higher than the provisional ones set out last year. This has led us to increase CDEL spending between 2021-22 and 2023-24 by £15.0 billion a year on average, despite assuming much greater underspends.

## Table 3.16: RDEL and CDEL spending and changes since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| PSCE in RDEL | | Implied, post-Spending Review | | | | |
| March 2019 forecast | | | | | | |
| Limits[1] | 314.7 | 327.1 | 336.8 | 347.1 | 359.3 | |
| Assumed underspend | -2.5 | -2.5 | -2.5 | -2.5 | -2.5 | |
| Actual spending | 312.2 | 324.6 | 334.3 | 344.6 | 356.8 | |
| March 2020 forecast | | | | | | |
| Limits[1] | 317.6 | 343.0 | 365.2 | 380.0 | 396.0 | 413.0 |
| Assumed underspend | -1.3 | -3.2 | -3.9 | -4.1 | -4.3 | -4.4 |
| Actual spending | 316.3 | 339.8 | 361.3 | 375.9 | 391.8 | 408.6 |
| Changes | | | | | | |
| Limits[1] | 2.9 | 16.0 | 28.4 | 32.8 | 36.7 | |
| Assumed underspend | 1.2 | -0.7 | -1.4 | -1.6 | -1.8 | |
| Actual spending | 4.1 | 15.2 | 27.0 | 31.2 | 34.9 | |
| PSGI in CDEL | | | Implied, post-Spending Review | | | |
| March 2019 forecast | | | | | | |
| Limits[1] | 63.0 | 68.0 | 72.8 | 75.2 | 79.4 | |
| Assumed underspend | -2.7 | -2.5 | -4.0 | -4.0 | -4.0 | |
| Actual spending | 60.3 | 65.5 | 68.8 | 71.2 | 75.4 | |
| March 2020 forecast | | | | | | |
| Limits[1] | 62.5 | 75.1 | 89.5 | 94.5 | 99.5 | 102.9 |
| Assumed underspend | -2.6 | -3.9 | -7.3 | -7.8 | -8.0 | -8.1 |
| Actual spending | 59.9 | 71.2 | 82.2 | 86.6 | 91.5 | 94.8 |
| Changes in actual spending | | | | | | |
| Limits[1] | -0.5 | 7.1 | 16.8 | 19.3 | 20.1 | |
| Assumed underspend | 0.1 | -1.4 | -3.3 | -3.8 | -4.0 | |
| Actual spending | -0.4 | 5.7 | 13.4 | 15.4 | 16.1 | |
| | Per cent of GDP | | | | | |
| PSCE in RDEL (actual spending) | | | | | | |
| March 2019 forecast | 14.2 | 14.3 | 14.2 | 14.1 | 14.1 | |
| March 2020 forecast | 14.2 | 14.7 | 15.1 | 15.2 | 15.3 | 15.4 |
| Change | 0.0 | 0.5 | 0.9 | 1.0 | 1.2 | |
| PSGI in CDEL (actual spending) | | | | | | |
| March 2019 forecast | 2.7 | 2.9 | 2.9 | 2.9 | 3.0 | |
| March 2020 forecast | 2.7 | 3.1 | 3.4 | 3.5 | 3.6 | 3.6 |
| Change | -0.1 | 0.2 | 0.5 | 0.6 | 0.6 | |

[1] In the years covered by the Spending Review, limits reflect the Departmental spending allocations agreed with HM Treasury at the latest Spending Review, adjusted for policy changes and classification changes since. In years beyond the Spending Review this reflects the implied limits consistent with what HM Treasury intends to spend and our view on underspends.

3.82 Table 3.17 details the sources of revisions to our forecast since March 2019, breaking them down between our underlying forecast judgements (which relate primarily to 2019-20) and the effects of the Government's decisions (which are large in most years).

3.83 In 2019-20 we have reduced the amount by which we expect RDEL plans to be underspent by £1.2 billion (thereby increasing actual spending). This reflects the final spending plans set at Supplementary Estimates, which reallocated some underspending, the latest in-year

evidence available to the Treasury, and past experience of how departments' own spending forecasts tend to evolve in the final months of the year. We have also nudged down our estimate of CDEL underspending in 2019-20 by £0.1 billion on a pre-measures basis.

3.84 From 2020-21 onwards, the Government has announced significant increases in RDEL and CDEL limits rising to £40.8 billion and £20.8 billion in 2024-25 respectively. The consequences for actual spending are tempered by our assumption that underspending relative to these materially higher limits will also be greater. Since detailed plans have not yet been set out, we have simply assumed that a fraction of the planned higher spending will be left unspent. For RDEL, we have assumed that 5 per cent of the additional funding is not spent, taking overall underspends between 2021-22 and 2024-25 from 0.7 to 1.0 per cent between the pre- and post-measures forecasts. For CDEL, we have assumed a much larger 20 per cent of the additional funding in each year is not spent, taking overall underspends from 4.7 to 7.5 per cent on average. This reflects past experience of attempts to ramp up capital spending sharply, as discussed in Box 3.2.

## Table 3.17: Sources of changes to DELs since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| PSCE in RDEL | | | | | | |
| March 2019 forecast | 312.2 | 324.6 | 334.3 | 344.6 | 356.8 | |
| March 2020 forecast[1] | 316.3 | 339.8 | 361.3 | 375.9 | 391.8 | 408.6 |
| Change | 4.1 | 15.2 | 27.0 | 31.2 | 34.9 | |
| *of which:* | | | | | | |
| Forecast changes | 1.2 | | | | | |
| Assumed underspend | 1.2 | | | | | |
| Effect of UK Government decisions[1] | 2.9 | 15.2 | 27.0 | 31.2 | 34.9 | 38.9 |
| Scorecard measures | 2.5 | 14.9 | 27.2 | 31.9 | 35.6 | 38.6 |
| Non-scorecard measures | 0.4 | 1.0 | 1.2 | 0.9 | 1.2 | 2.2 |
| Assumed underspend | 0.0 | -0.7 | -1.4 | -1.6 | -1.8 | -1.9 |
| PSGI in CDEL | | | | | | |
| March 2019 forecast | 60.3 | 65.5 | 68.8 | 71.2 | 75.4 | |
| March 2020 forecast[1] | 59.9 | 71.2 | 82.2 | 86.6 | 91.5 | 94.8 |
| Change | -0.4 | 5.7 | 13.4 | 15.4 | 16.1 | |
| *of which:* | | | | | | |
| Forecast changes | 0.1 | 0.0 | | | | |
| Assumed underspend | 0.1 | 0.0 | | | | |
| Effect of UK Government decisions[1] | -0.5 | 5.7 | 13.4 | 15.4 | 16.1 | 16.7 |
| Scorecard measures | 0.0 | 7.0 | 16.7 | 19.2 | 20.0 | 20.7 |
| Non-scorecard measures | -0.5 | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 |
| Assumed underspend | 0.0 | -1.4 | -3.3 | -3.8 | -4.0 | -4.1 |

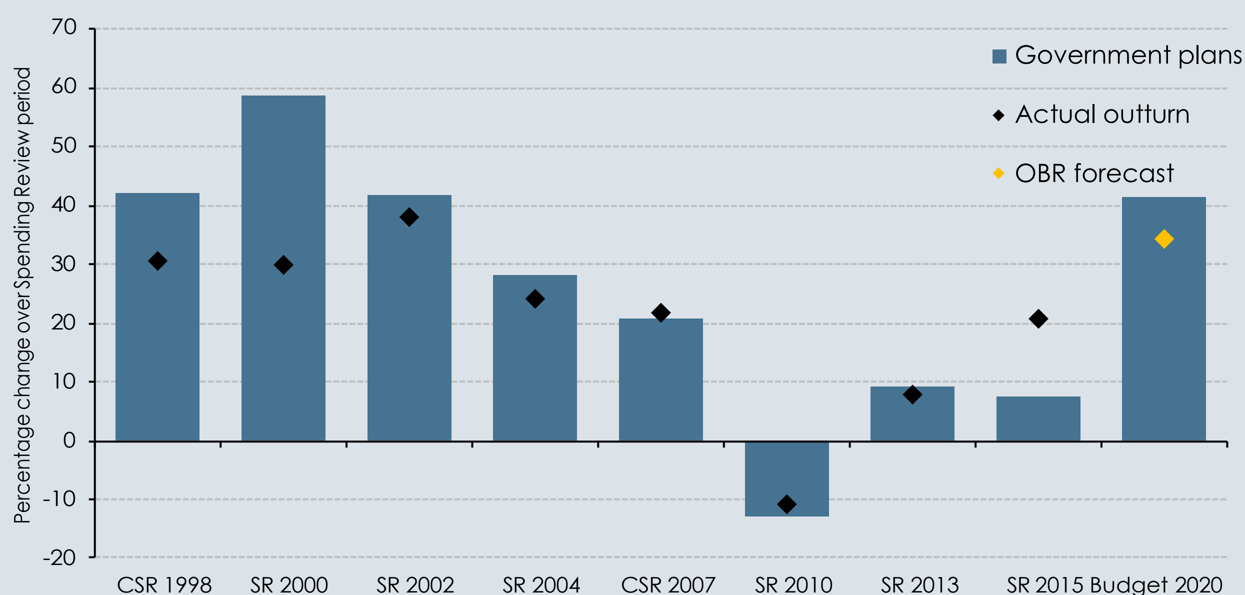
[1] The change in 2024-25 is relative to a baseline that assumes DEL would otherwise have remained constant as a share of GDP.

## Box 3.2: Capital spending plans: how much will actually be spent?

When presented with DEL limits for capital spending in a Budget or other fiscal statement, we need to decide what that they imply for the *actual* level of spending and the budget deficit. History shows that departmental capital budgets are almost always underspent, so in our forecasts we always assume some degree of underspending in each year.

More importantly for the judgement that we have to make in this particular forecast, history also shows that ramping capital spending up quickly is particularly difficult, implying larger underspends than when spending limits evolve relatively smoothly. This was true in the pre-crisis decade under the Labour Government, when capital spending growth fell short of plans in most Spending Reviews (Chart A). Actual capital spending did exceed the plans set out in the 2007 Comprehensive Spending Review and 2015 Spending Review, but in both cases this was due to subsequent deliberate policy decisions to loosen fiscal policy. The cuts to capital spending set out in the 2010 Spending Review were also partly reversed by subsequent policy decisions.

### Chart A: Capital spending plans versus outturn at successive Spending Reviews




Note: Capital spending is defined as public sector gross investment. Outturn is taken from the March/April forecast of the following financial year to minimise the impact of classification changes.
Source: OBR

Given the frequent changes made to the composition of Capital DELs and the lack of sufficient long-run historical outturn series, we have calibrated our underspend assumptions by looking at differences between forecast and outturn for public sector gross investment in the period from 1998 to 2007, when the Labour Government was seeking to raise public investment as a share of GDP. We have employed the same methodology used by the Institute for Fiscal Studies in its recent study of public spending control,[a] taking 'outturn' from Budgets a year after the year in question, so that they are less affected by subsequent classification changes.

As Table B shows, outturn spending fell short of plans at the one-, two- and three-year horizons in every forecast during this period. The average percentage error against plans was around 10 per cent at each of these horizons. This period followed sustained falls in public investment as a

share of GDP, so the planned increases required a significant change of direction. That contrasts with the increases announced in this Budget, which come on top of an already rising trend. On this basis, we have assumed that underspending against the new totals will be somewhat lower than implied by the pre-crisis Labour years. Specifically, we have assumed that 20 per cent of the addition to plans relative to the pre-measures forecast will be underspent, which implies that around 8 per cent of total CDEL plans will go unspent each year.

### Table B: Outturn versus plans for capital spending:1998-99 to 2006-07

| | In-year | 1 year ahead | 2 years ahead | 3 years ahead |
|---|---|---|---|---|
| Number of forecasts | 22 | 22 | 20 | 12 |
| *of which:* | | | | |
| Spending fell short of forecast | 19 | 22 | 20 | 12 |
| Spending exceeded forecast | 3 | 0 | 0 | 0 |
| Average percentage error | -7 | -10 | -11 | -8 |

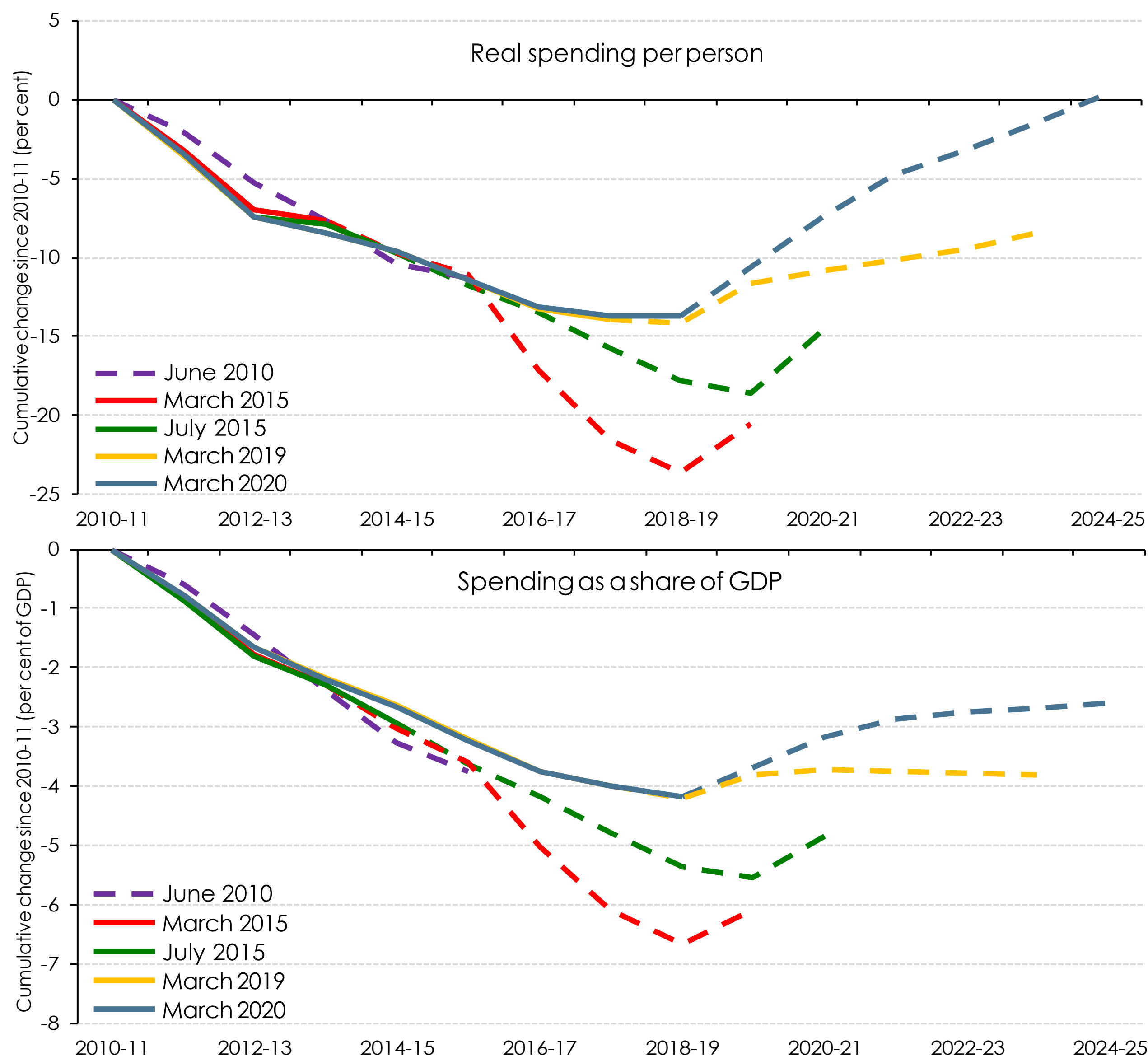
[a] *The planning and control of UK public expenditure, 1993–2015*, Crawford, Johnson and Zaranko, July 2018.

## The fall and rise of DEL spending since 2010-11

3.85 DEL spending relates to England, Wales and Northern Ireland, with the Treasury now managing equivalent Scottish spending via AME. Despite this, it covers largely the same activities and is set in largely the same way – with large increases announced in the Budget reflecting the large increases in RDEL and CDEL. In this section we look at both combined.

3.86 Chart 3.2 shows the striking turnaround in the path of resource spending by central government departments across the UK set out in this Budget. Viewed in terms of real spending per person, the eight years of cuts from 2010-11 are entirely reversed by 2024-25, with almost half reversed just this year and next. The increased resource spending announced in this Budget, in last year's Spending Round and in the NHS settlement of June 2018, continue the change in the spending tide that started in the Summer Budget of July 2015, when the newly elected Conservative Government moderated the sharp cuts in RDEL spending previously pencilled into the March 2015 pre-election Budget. But, viewed as a share of GDP, only around a third of the cuts will have been reversed by 2024-25.

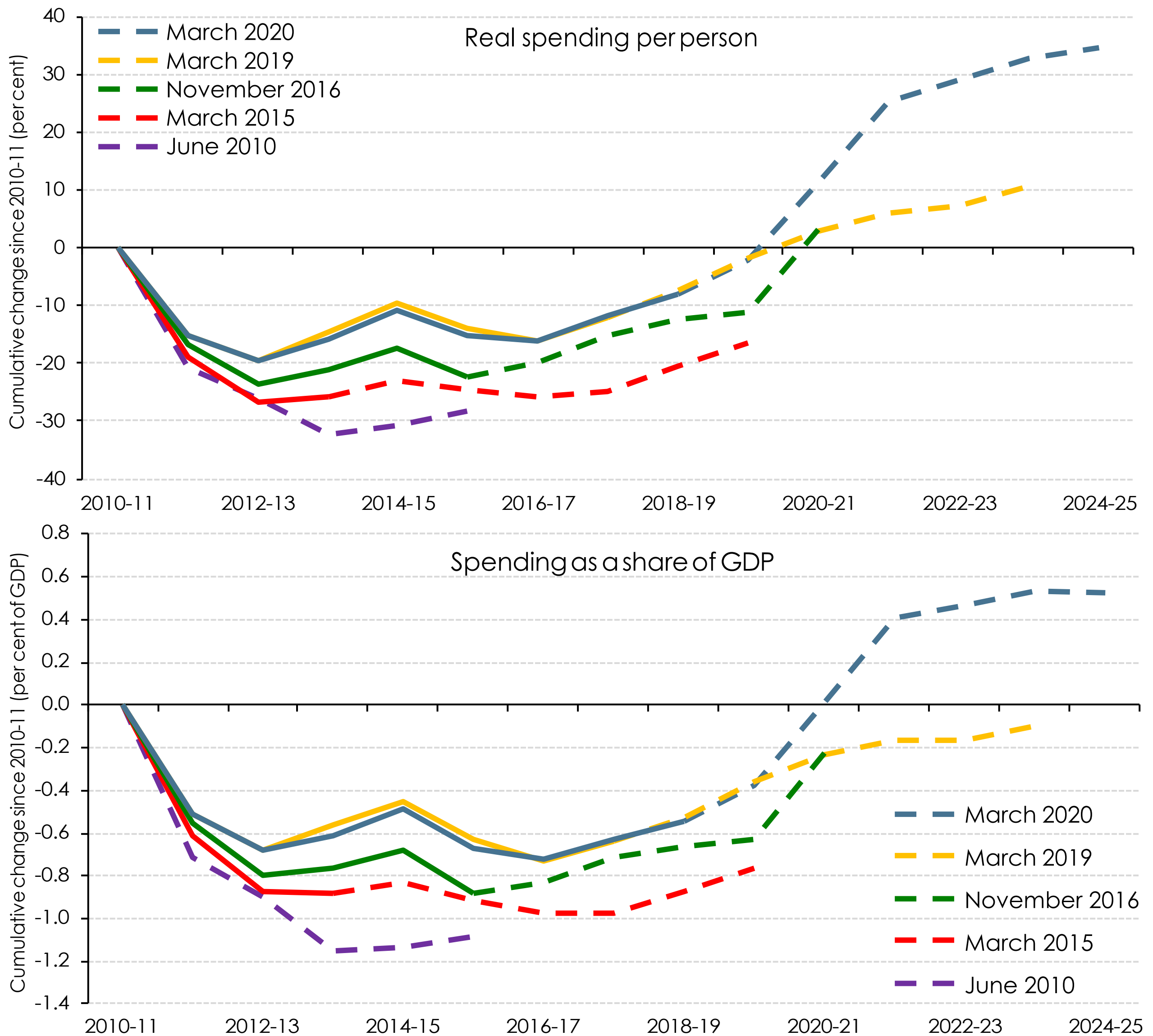
## Chart 3.2: Change in RDEL spending since 2010-11




Note: 2017-18 and 2018-19 exclude the effects of business rates pilots. All other figures include both RDEL and Scottish Government current AME and are adjusted as far as possible for consistency with the latest forecast. See source table in the supplementary expenditure tables on our website.
Source: OBR

3.87 Chart 3.3 shows the same spending paths for departmental capital spending. The profile differs from that of resource spending, in that the sharp cuts implemented in the first two years of the Coalition Government (that had been a feature of the previous Labour Government's March 2010 Budget plans) were already being slowly reversed over the subsequent six years. By 2020-21 they will have been more than reversed, thanks largely to increases announced in the 2016 Autumn Statement. The additional increases announced in this Budget would, given our underspend assumptions, leave real CDEL spending per person in 2024-25 around 35 per cent higher than it was in 2010-11 and more than 50 per cent higher than the low it reached in 2012-13. As a share of GDP, CDEL spending remained below its 2010-11 level in our last forecast, but now rises above it in 2021-22.

## Chart 3.3: Change in CDEL spending since 2010-11




Note: 2017-18 and 2018-19 exclude the effects of business rates pilots. All other figures include both CDEL and Scottish Government capital AME and are adjusted as far as possible for consistency with the latest forecast. See source table in the supplementary expenditure tables on our website.
Source: OBR

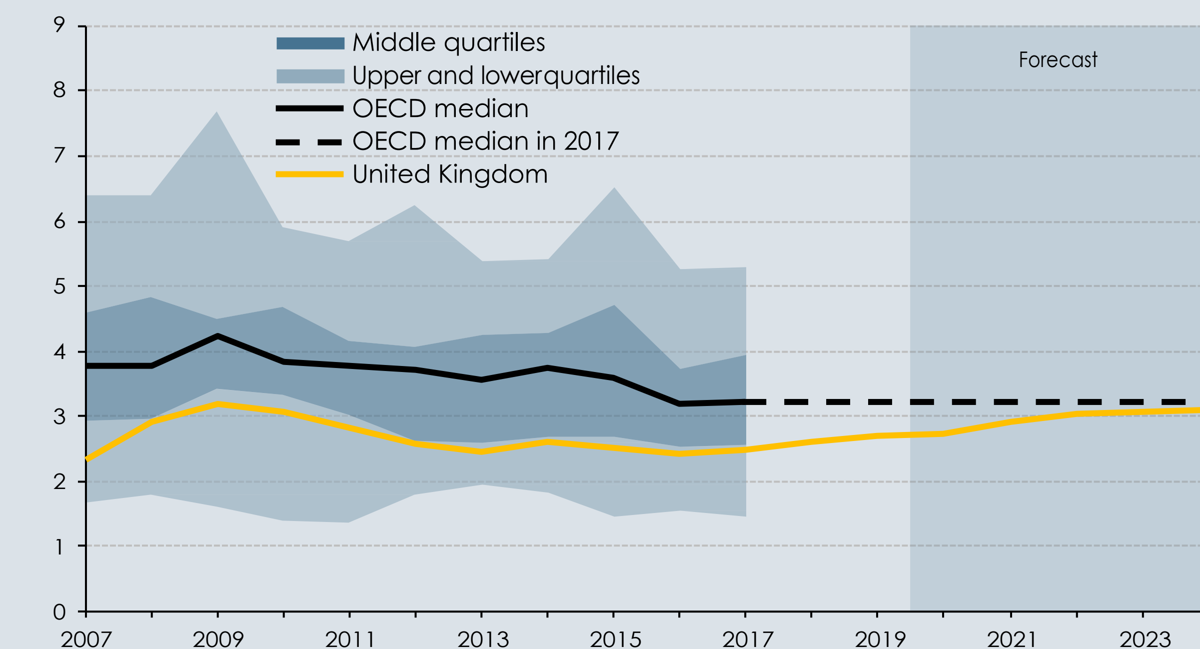
### Box 3.3: International comparisons of government investment

Measured on an internationally comparable basis,[a] the capital spending increases announced in this Budget will take government investment from 2.5 per cent of GDP in 2017 to 3.1 per cent of GDP in 2024. But how does that compare with other advanced economies?

Chart B shows the UK's relative position among 30 OECD countries over the decade to 2017.[b] Across the whole period, the UK was consistently positioned within the bottom quarter in terms of government investment as a share of GDP – more specifically, it was ranked between 23rd and 27th out of 30 countries in every year. UK government investment was a little higher as a share of GDP in 2017 than in 2007, having first risen during the crisis then fallen back. The large increase over the next five years will take it to around the present OECD median. But it will still

fall well short of levels in countries whose governments invested most over the past decade – in South Korea, Estonia and Latvia investment averaged around 5 per cent of GDP a year.

### Chart B: UK government investment on an internationally comparable basis relative to other OECD countries




Source: OBR

[a] Using OECD data at the level of general government (i.e. central and local government in the UK, plus state governments in countries that have them) and the National Accounts metric of gross capital formation plus acquisitions less disposals of valuables.
[b] Our analysis comprises 30 out of 36 OECD member countries; data on the OECD statistics website is unavailable in the required format for Canada, Chile, Iceland, Mexico, New Zealand, and Turkey.

## Annually managed expenditure

### Welfare spending

3.88 Total welfare spending in our forecast refers to AME spending on social security and tax credits. Just over half is subject to the Government's 'welfare cap', which excludes the state pension and those payments most sensitive to the economic cycle. We provide an update on performance against the cap in Chapter 4.

3.89 As detailed in our 2018 *Welfare trends report (WTR)*, much of our working-age welfare spending forecast is constructed by estimating a counterfactual in which the 'legacy' benefits system continues as though universal credit (UC) did not exist, and then adding to it an estimate of the marginal cost associated with rolling UC out. This has allowed us to base the forecast on as much administrative data as possible, but it does not directly reflect the real-world change in spending on legacy benefits as spending on UC rises. For the year in progress, we forecast on an 'actual cost' basis, since the counterfactual and marginal effects cannot be observed in the monthly flow of administrative data. This approach generates several problems that add uncertainty to our forecasts, but is unavoidable at present. As soon as is practical, we will switch to forecasting UC on an actual cost basis in all years.

3.90 Table 3.18 shows our latest welfare spending forecasts split into broad recipient groups.[11] It includes the disability benefits spending in Scotland that has been devolved and will in future be subsumed within the Scottish Government's overall AME budget. It shows that welfare spending is forecast to increase by 19 per cent in cash terms between 2019-20 and 2024-25, but to remain flat as a share of GDP. Spending within the welfare cap is expected to fall relative to GDP, while spending outside the cap – which is dominated by state pensions – is projected to rise as a share of GDP from 2020-21 onwards as the ageing population raises state pensions spending during a period in which there are no offsetting downward pressures from increases in the State Pension age.

## Table 3.18: Total welfare spending

| | £ billion | | | | | | |
|---|---|---|---|---|---|---|---|
| | | Forecast | | | | | |
| | Outturn | | Welfare cap period | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Pensioner spending[1] | 109.7 | 111.7 | 114.7 | 119.0 | 124.5 | 130.6 | 136.9 |
| UC and legacy equivalents[2] | 63.5 | 64.0 | 66.5 | 67.2 | 68.7 | 70.6 | 71.9 |
| Disability benefits[3] | 24.4 | 25.9 | 26.9 | 28.2 | 29.5 | 31.0 | 32.2 |
| Child benefit | 11.6 | 11.5 | 11.6 | 11.8 | 12.0 | 12.1 | 12.2 |
| Other spending[4] | 13.7 | 14.3 | 14.7 | 15.3 | 16.0 | 16.7 | 17.5 |
| Effect of government decisions | 0.0 | 0.0 | -0.2 | -0.5 | -0.7 | -1.3 | -1.0 |
| Budget 2020 welfare devolution | 0.0 | -2.7 | -2.8 | -2.9 | -3.0 | -3.2 | -3.3 |
| Indirect effect of government decisions | 0.0 | 0.0 | -0.2 | -0.4 | -0.1 | 0.3 | 0.5 |
| Total welfare spending[5] | 222.8 | 224.6 | 231.2 | 237.8 | 246.8 | 256.9 | 266.8 |
| *of which:* | | | | | | | |
| Inside welfare cap | 119.5 | 119.0 | 122.6 | 124.3 | 127.0 | 130.2 | 133.5 |
| Outside welfare cap | 103.3 | 105.6 | 108.6 | 113.5 | 119.8 | 126.7 | 133.4 |
| | Per cent of GDP | | | | | | |
| Total welfare spending[5] | 10.3 | 10.1 | 10.0 | 9.9 | 10.0 | 10.0 | 10.1 |
| *of which:* | | | | | | | |
| Inside welfare cap | 5.5 | 5.3 | 5.3 | 5.2 | 5.1 | 5.1 | 5.0 |
| Outside welfare cap | 4.8 | 4.7 | 4.7 | 4.7 | 4.8 | 4.9 | 5.0 |

[1] Pensioner spending includes pensioner housing benefit, pension credit, state pension expenditure and winter fuel payments.
[2] UC and legacy equivalents includes personal tax credits, housing benefit (excluding pensioner part), incapacity benefits, contributory ESA, income support and income-based and contributory jobseeker's allowance.
[3] Disability benefits includes disability living allowance, personal independence payment, and attendance allowance. It also includes the equivalent spending that is devolved to Scotland.
[4] Other spending includes all Northern Ireland social security expenditure.
[5] Total welfare outturn inside and outside of the welfare cap in 2018-19 is sourced from OSCAR, consistent with PESA 2019. For 2018-19 only, the components reflect departments' own outturns, which may not be on a consistent basis to OSCAR. For this year the components may not sum to the total for this reason.

3.91 Table 3.19 sets out the sources of changes to welfare spending since our March 2019 forecast, again abstracting from the effect of devolving Scottish disability benefits spending. We have revised total spending up significantly from 2020-21 onwards, mainly in respect of working-age benefits, but also pension credit. This is offset somewhat by progressively larger downward revisions to spending on disability benefits and on state pensions.

[11] Forecasts for individual benefits are available in a supplementary table on our website.

3.92 On a pre-measures basis, our lower inflation forecast has led to progressively larger downward revisions thanks to lower CPI uprating and therefore lower average awards. We have also made some relatively large, but partly offsetting, modelling changes:

- Universal credit and its legacy predecessors. Spending has been revised up by progressively larger amounts, reaching £4.9 billion in 2023-24. This is almost entirely due to a change in our assumption regarding growth in incapacity benefits and housing benefit among people who are unable to work due to sickness or disability. We now assume that the caseload rises in line with the working-age population, reflecting the turnaround over the past year of the long-standing decline in the prevalence of benefit receipt from its mid-2000s peak. Spending on personal tax credits has also been revised up, partly due to lower than expected earnings growth for tax credit recipients in the latest outturn data and increased out-of-work caseloads.

- Pension credit. Spending has been revised up significantly, reflecting the BBC's announcement in June 2019 that it would means-test TV licences for over-75s by providing free licences only to those receiving pension credit. We assume that this will increase take-up, adding £0.6 billion a year on average from 2020-21 onwards.[12]

- State pensions. Spending has been revised down by progressively larger amounts due to the higher mortality rates reflected in the latest ONS population projections. This lowers the caseload by 75,000 in 2023-24 relative to our March 2019 forecast, reducing spending by £0.6 billion in that year. (Higher mortality rates have also lowered our forecasts for other pensioner benefits, such as winter fuel payments.)

- Disability benefits. We have revised spending down by £0.6 billion a year on average, largely reflecting much lower than expected costs from recent legal rulings.

- Other welfare spending has also been revised down, including statutory maternity pay (due to fewer births and lower outturn), carer's allowance (due to fewer in receipt of disability benefits) and tax-free childcare (due to lower-than-expected take-up).

3.93 In terms of Budget measures, the managed migration phase of UC has been pushed back again and we have assumed it will take two years longer than DWP currently assumes (rather than the six-month delay we have assumed in recent forecasts, as discussed below). Overall, this lowers spending by £0.6 billion a year on average between 2022-23 and 2024-25 as less is spent on transitional protection for those who lose out when moving to UC from the legacy system at DWP's behest. Other Budget measures have smaller effects. These include slowing the final phase of transferring claimants from disability living allowance to personal independence payment and restricting access to various benefits for EU migrants until they have been granted indefinite leave to remain by the Home Office (typically after five years' residence).

[12] This was discussed in Box 5.1 of our 2019 *Fiscal risks report*.

3.94 Other policy-related effects on welfare spending include:

- The effect of the Budget package on the economy has largely offsetting effects, with higher earnings growth raising state pensions spending via the triple lock but reducing means-tested benefits spending via its effects on claimants' incomes. Temporarily higher CPI inflation raises working-age spending via higher uprating.
- The new migration regime lowers spending by progressively larger amounts, reaching £0.5 billion in 2024-25. This represents a 0.4 per cent reduction in the cost of working-age and child benefits, in line with the 0.4 per cent drop in the working-age population that we have assumed will result from the new regime (see Box 3.6).
- Raising the National Living Wage has a largely neutral effect on welfare, with working age benefits pushing spending down through higher incomes, but with the offsetting effect of higher earnings increasing state pensions spending via the triple lock.

3.95 The devolution of disability benefits to Scotland has shifted £2.9 billion a year on average from welfare spending to Scottish Government AME. We have abstracted from that here.

## Table 3.19: Sources of change to welfare spending since March 2019

| | £ billion | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Total welfare spending | | | | | | | |
| March 2019 forecast | 223.0 | 227.3 | 232.2 | 240.0 | 249.5 | 260.5 | |
| *less* Budget 2020 welfare devolution | 0.0 | -2.7 | -2.8 | -2.9 | -3.0 | -3.2 | |
| Restated March 2019 forecast | 223.0 | 224.6 | 229.4 | 237.1 | 246.5 | 257.3 | |
| March 2020 forecast | 222.8 | 224.6 | 231.2 | 237.8 | 246.8 | 256.9 | 266.8 |
| Change | -0.2 | 0.0 | 1.8 | 0.7 | 0.4 | -0.4 | |
| *of which:* | | | | | | | |
| Forecast changes | -0.2 | 0.0 | 2.2 | 1.5 | 1.2 | 0.6 | |
| CPI inflation | 0.0 | 0.0 | -0.6 | -1.3 | -1.6 | -1.8 | |
| UC and legacy equivalents modelling[1] | 0.3 | 0.8 | 3.4 | 3.8 | 4.4 | 4.9 | |
| Pension credit modelling | 0.0 | 0.2 | 0.5 | 0.7 | 0.6 | 0.5 | |
| State pension modelling | 0.0 | 0.0 | -0.2 | -0.4 | -0.7 | -1.1 | |
| Disability benefits modelling[2] | 0.0 | -0.5 | -0.5 | -0.5 | -0.6 | -0.8 | |
| Other factors | -0.4 | -0.4 | -0.5 | -0.7 | -0.9 | -1.2 | |
| Effects of Government decisions | 0.0 | 0.0 | -0.4 | -0.8 | -0.8 | -0.9 | -0.5 |
| Budget measures[3] | 0.0 | 0.0 | -0.2 | -0.5 | -0.7 | -1.3 | -1.0 |
| Indirect effects | 0.0 | 0.0 | -0.2 | -0.4 | -0.1 | 0.3 | 0.5 |
| *of which:* | | | | | | | |
| Due to tax and spending measures | 0.0 | 0.0 | -0.2 | -0.2 | 0.1 | 0.7 | 0.9 |
| Raising the National Living Wage | 0.0 | 0.0 | 0.0 | -0.1 | -0.1 | -0.1 | 0.0 |
| New migration regime | 0.0 | 0.0 | 0.0 | 0.0 | -0.1 | -0.3 | -0.5 |

[1] UC and legacy equivalents includes personal tax credits, housing benefit (excluding pensioner part), incapacity benefits, contributory ESA, income support and income-based and contributory jobseeker's allowance.

[2] Disability benefits includes disability living allowance, personal independence payment, and attendance allowance.

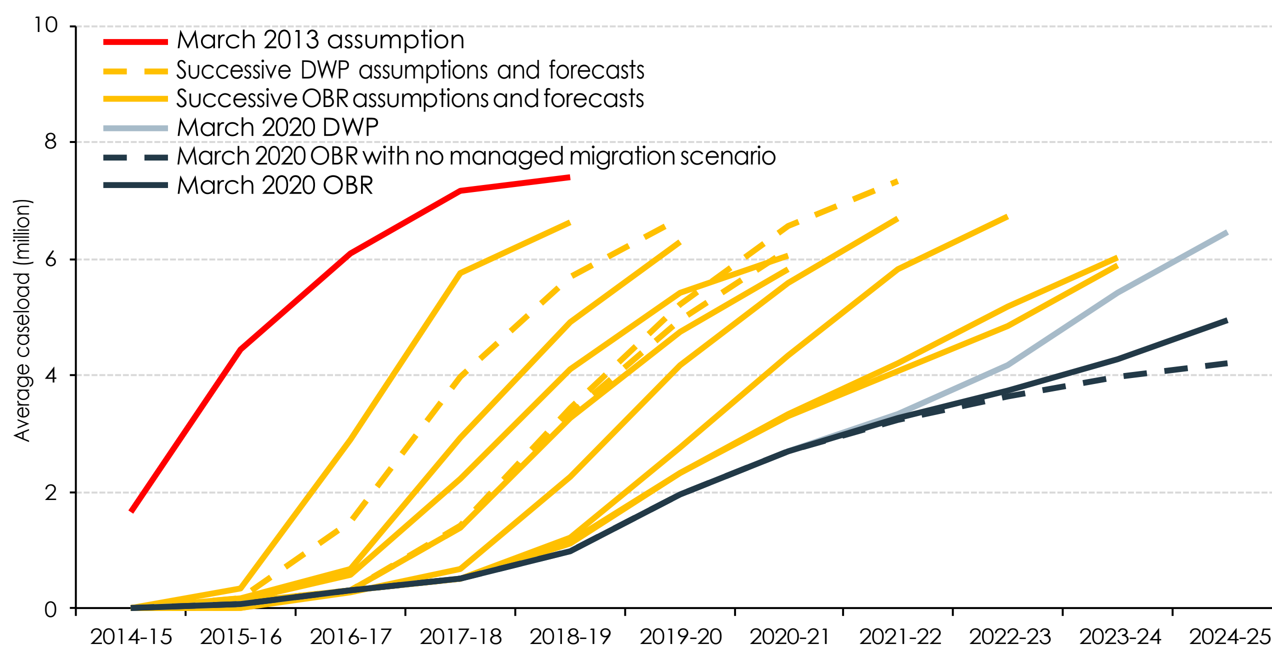
[3] This excludes the impact of the Budget 2020 welfare devolution measure.

### The rollout of universal credit

3.96 Ever since our December 2014 *EFO*, we have assumed that the rollout of UC will take longer than DWP's own plans assume. In that time, we have always assumed a six-month delay, although its precise terms have changed as the rollout itself has evolved. As of March 2019, with UC rolled out to all jobcentres for new claims, we assumed that the managed migration phase would start on time but take six months longer to complete than DWP assumed. But in February 2020, DWP Ministers announced that a slower pace of natural migrations to UC meant that 900,000 more cases would need to be migrated by DWP and so the rollout would take nine months longer than previously assumed – ending in September 2024 rather than December 2023. In terms of our own assumptions, that means shifting from a June 2024 end-point to September 2026 (beyond our forecast horizon). As Chart 3.4 shows, whereas DWP's plans imply 6.5 million UC cases in 2024-25, our rollout assumptions imply 4.9 million. That is still higher than the 4.2 million that would move to UC naturally through changes of circumstance or new claims by 2024-25 in the absence of further managed migrations once the current pilot phase is completed.

3.97 Our decision to diverge more materially from DWP's plans reflects both the accumulated experience of the past seven years – illustrated in Chart 3.4 – and the greater emphasis apparent in recent statements from DWP Ministers on taking things slowly to protect claimants.[13] It has always been difficult to forecast the UC rollout given the 'test and learn' approach being taken, which is naturally more prone to delay than acceleration. Our six-month assumption has repeatedly been overtaken by events, so we have chosen two years as a period around which we hope the risks will be more evenly balanced.

### Chart 3.4: Successive revisions to the universal credit rollout assumption




Source: DWP, OBR

[13] For example, on 4 February when debating the latest rollout delay in Parliament, the Parliamentary Under-Secretary of State for Work and Pensions assured the House that "*as we move into the managed migration phase protecting the vulnerable will be our utmost concern.*" On 27 January, when answering questions about the slow start to the managed migration pilot in Harrogate, he said that "*My clear instruction to officials was to take this slow and steady, and to go at the pace the claimant requires.*"

3.98 As well as the well-documented risks to the pace at which UC is rolled out – and especially the managed migration phase – the continued rollout to eligible families is making it increasingly difficult to interpret the flow of administrative spending data. Given the scale of spending on UC and its equivalents in the legacy system, this is a material source of risk to our welfare spending and wider fiscal forecasts. Box 3.4 discusses the nature of these risks.

## Box 3.4: Interpreting surprises in spending on UC and its legacy equivalents

When preparing our fiscal forecasts, we are inevitably faced with surprises in the latest data relative to what would have been consistent with our most recent published forecast. How we interpret these surprises helps shape the revisions to our medium-term forecasts. That places a premium on being able to scrutinise the flow of administrative data against the assumptions underpinning our forecasts so that we can identify the source of upside or downside surprises.

For the £64.0 billion of spending on UC, and its legacy equivalents in 2019-20, that is extremely difficult. Analysis is hampered by the less than ideal, but unavoidable, way in which the forecast is constructed, and by uncertainties around the UC rollout. As detailed in our 2018 *Welfare trends report*, to understand the likely future trends in the UC claimant base it is essential to analyse and interpret past and present trends in the same base receiving legacy benefits, which requires us to be able to group claimants in a comparable way across both systems.

By way of illustration, if we were faced with a 1 per cent upside surprise in spending in the year in progress – i.e. around £0.6 billion, close to the upward revision we have made in this forecast – we would broadly have four alternative ways to interpret it, namely as:

- A one-off event that will reverse next year. For example, if a build-up of arrears was identified and paid out, we would know that this would not be repeated in future. This would imply a 1 per cent fall in spending next year and not affect spending in 2024-25.
- A one-off event that will persist. For example, if CPI uprating was 1 percentage point higher than assumed in the previous forecast. This would raise spending in every year by the same proportion, so in 2024-25 we would revise it up by £0.7 billion.
- News about the cost of UC relative to the legacy system. UC is expected to cost more than the legacy system, with the net additional cost reflecting large and offsetting gross costs and savings associated with different types of UC cases. If the upside spending surprise were interpreted as a higher marginal cost of UC – perhaps because take-up of UC was higher than assumed – then it might be expected to build up at the same pace as the UC rollout progresses. Our latest forecast assumes that around a third of the eventual UC caseload will already have moved to UC in 2019-20 and that three quarters will have moved by 2024-25, so a 1 per cent surprise this year would imply a 2.5 per cent upward revision in 2024-25 – £1.8 billion.
- News about the rate of spending growth. For example, it might appear that previous assumptions about trends in the prevalence of benefit receipt among the working-age population were too low. If this translated into spending growth being 1 percentage point higher each year, it would be revised up by 6.2 per cent in 2024-25 (£4.4 billion).

In some cases, it is relatively simple to interpret news. DWP knows how much it has spent addressing past underpayments, although there is much more uncertainty over how much future arrears payments will cost. And we know how actual uprating differs from the assumptions in our previous forecast. But in many cases it is much harder to attribute changes in spending to these individual interpretations. DWP analysts try to assess what the actual UC caseload would have looked like under the legacy system and to understand whether surprises in actual UC spending relate to surprises in the pace of rollout, in the take-up of UC relative to the legacy benefits, or in the amounts awarded relative to the amounts predicted by forecast models. This often proves particularly difficult for UC cases that bear most resemblance to HMRC-administered tax credits cases in the legacy system. Unfortunately, it is still difficult to track whether, and how, claimants leaving the tax credits system have moved into the UC system. And we cannot know who would have made a new claim to tax credits but now claims UC instead.

These inevitable difficulties are compounded by problems we have in interrogating the UC forecast. For example, management information is not routinely mapped onto forecast assumptions to test their veracity, while DWP's modelling of the flows associated with our judgements about the stock of different cases – essential to understanding the UC rollout – involves a particularly cumbersome process. These and other factors mean that it is often almost impossible to judge with confidence whether news this year should affect assumptions about the level or growth of the legacy counterfactual forecast or the UC marginal cost.

We have revised UC and legacy equivalent spending in 2023-24 up by £4.9 billion in this forecast – essentially a 'spending growth' interpretation of news about the incapacity benefits caseload. The examples above show how different interpretations of equally-sized surprises could result in very different revisions to future medium-term forecasts.

## Locally financed current expenditure

3.99 We forecast spending by local authorities by forecasting their sources of income – including grants from central government and local sources – and the extent to which they will then overspend or underspend that income by varying their reserves or borrowing. Our forecast therefore encompasses spending financed by grants, which are mostly in DELs, and locally financed expenditure, which is in AME. Tables 3.20 and 3.21 focus on locally financed expenditure. Further detail is available in supplementary tables on our website.

3.100 Table 3.20 summarises the main changes to our locally financed current expenditure forecast since March 2019. When looking at these changes, it is important to distinguish between those related to council tax and business rates – which also affect our receipts forecast and are therefore broadly neutral for borrowing – and those related to the net use of reserves or changes in the amounts set aside to repay debt. These reflect authorities spending more or less than their income and therefore affect our borrowing forecast.

3.101 We have not changed our overall judgement about the amount that local authorities will use their reserves in 2019-20. But within this total we expect Transport for London (TfL) to make a one-off drawdown of £0.7 billion, offset by an addition to reserves across other English

authorities. We then assume that non-TfL English authorities taper net additions to reserves to zero by 2022-23.

3.102 Other changes to our forecast include a revised forecast of the effects of the 2020-21 business rates revaluation, which adds £0.5 billion to spending in 2020-21 declining to less than £0.1 billion by the end of the forecast due to the assumed path of successful appeals. Offsetting that, general fund income growth has been revised down based on the latest local authority budgets, lowering spending by around £0.4 billion a year.

3.103 Budget measures raise locally financed spending overall. These include:

- Business rates retention pilots in devolution deal areas and Greater London Authority boosts locally financed current expenditure by around £1.7 billion in 2020-21 at the expense of forgone expenditure financed by grants from central government.
- The increase in the amount by which English authorities with social care responsibilities can increase the adult social care precept rates without calling a local referendum from 2 per cent to 4 per cent in 2020-21. This adds £0.5 billion a year to spending from 2020-21 onwards (and boosts receipts in equal measure).
- A number of small measures on business rates and the current expenditure consequences of changes to the Public Works Loan Board (PWLB) interest rate changes, which combined reduce expenditure by around £0.1 billion a year.

3.104 There are several sources of uncertainty around our local authority spending forecast that we discussed in our March 2018 *EFO* (in paragraph 4.129) and that remain relevant. They include continuing budget pressures, the sectoral shifts that result from converting schools into academies and replacing housing benefit with universal credit, and policy risks associated with future changes to business rates retention by local authorities.

## Table 3.20: Key changes to locally financed current expenditure since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| March 2019 forecast | 54.2 | 53.1 | 55.1 | 56.9 | 58.6 | |
| March 2020 forecast | 53.9 | 55.0 | 55.1 | 56.9 | 58.6 | 60.1 |
| Change | -0.4 | 1.9 | -0.1 | 0.0 | 0.0 | |
| *of which, changes in sources of local finance:* | | | | | | |
| Forecast changes | -0.4 | -0.2 | -0.6 | -0.5 | -0.5 | |
| Council tax | -0.1 | -0.1 | -0.1 | -0.1 | -0.1 | |
| Retained business rates | 0.0 | 0.5 | 0.0 | -0.1 | 0.0 | |
| Net use of current reserves | 0.0 | -0.2 | -0.1 | 0.0 | 0.0 | |
| Net general fund income | -0.4 | -0.3 | -0.3 | -0.3 | -0.4 | |
| Other | 0.1 | -0.1 | -0.1 | 0.0 | 0.1 | |
| Effect of Government decisions | 0.0 | 2.1 | 0.5 | 0.5 | 0.4 | 0.4 |

## Locally financed and public corporations' capital expenditure

3.105 Our latest forecasts for locally financed capital expenditure and public corporations' capital expenditure are shown in Table 3.21. These are net of asset sales, forecasts for which are available in supplementary tables on our website. Locally financed capital expenditure is measured net of capital spending by authorities' housing revenue accounts (HRAs) and Transport for London's subsidiaries; in both cases, these are treated as public corporations in the National Accounts.[14] So we switch these items from locally financed to public corporations' capital expenditure in our forecast to ensure consistency.

3.106 We present changes to locally financed and public corporations' capital expenditure together, so that switches such as those mentioned above net out and do not obscure the changes that affect TME. Spending has been revised up across the forecast period relative to our March 2019 forecast, by £2.3 billion in 2019-20, rising to £3.4 billion in 2023-24.

3.107 The main change to our pre-measures forecast is an upward revision to the level of capital spending financed by prudential borrowing that we expect (non-TfL) English authorities to undertake. This is based on analysis of local authorities' take-up of Public Works Loan Board (PWLB) loans, which has risen considerably, and on consultation with sector experts regarding forthcoming pressures on local authorities' capital spending budgets on refurbishing housing stock and the extent of further commercial investments.

3.108 This is an area of considerable uncertainty, as data on authorities' behaviour is lagged and we need to predict behaviour across many decision-makers, whose circumstances vary considerably. Our assessment points towards higher borrowing than previously thought, so we have increased our forecast by £2.3 billion by 2023-24.

3.109 Other sources of change to our forecast since March 2019 include:

- Upward revisions to spending financed by the major repairs reserve by around £0.5 billion each year, reflecting higher planned spending to refurbish housing stock.
- Upward revisions to our forecast for spending financed by capital receipts from sales, including 'right to buy' that rise to £0.6 billion in 2023-24, as a result of higher outturn data on the use of capital receipts and higher house prices.
- A forecast for asset sales lower by £0.5 billion in 2019-20, based on the outturn data for the first three quarters of the year. This increases net capital expenditure.
- Capital spending by TfL has been shifted from 2019-20 into later years, reflecting the latest delays in the opening of Crossrail.

3.110 The Government has announced various changes to interest rates charged on PWLB lending to local authorities. In October it raised the standard rate by 1 percentage point to 1.8

[14] These TfL transport subsidiaries trade under the company name 'Transport Trading Ltd' (TTL). The ONS currently classifies all the large TTL subsidiaries as public corporations apart from Crossrail, which is classified as part of the local government sector.

percentage points above gilt rates. In this Budget it has eased the effect of that change with lower rates for HRA borrowing and a new tranche of even lower rates for infrastructure projects. The net effect of these is to reduce local authority capital spending modestly. Additionally, the capital spending consequences of the business rates retention pilots increase spending by £0.3 billion in 2020-21.

## Table 3.21: Key changes to locally financed capital expenditure and public corporations' capital expenditure since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| March 2019 forecast | 21.9 | 19.8 | 19.3 | 19.1 | 18.6 | |
| March 2020 forecast | 24.1 | 22.3 | 21.6 | 22.3 | 21.9 | 22.4 |
| Change | 2.2 | 2.5 | 2.3 | 3.2 | 3.3 | |
| *of which:* | | | | | | |
| Forecast changes | 2.3 | 2.3 | 2.5 | 3.3 | 3.4 | |
| Prudential borrowing (non-TfL) | 1.0 | 1.4 | 1.9 | 2.1 | 2.3 | |
| Major repairs reserve | 0.5 | 0.5 | 0.5 | 0.6 | 0.6 | |
| Capital receipts from sales | 0.3 | 0.4 | 0.4 | 0.5 | 0.6 | |
| *Less* asset sales | 0.5 | -0.2 | -0.3 | -0.3 | -0.3 | |
| TfL capital spending | -0.2 | 0.0 | 0.1 | 0.1 | 0.0 | |
| Other | 0.2 | 0.1 | -0.1 | 0.3 | 0.3 | |
| Effect of Government decisions | -0.1 | 0.2 | -0.1 | -0.1 | -0.1 | -0.1 |

### Public sector debt interest

3.111 Debt interest payments are forecast by applying appropriate interest rates to the stocks of conventional and index-linked gilts outstanding at different maturities and to other debt, such as NS&I products and Treasury bills.[15] The assumptions we use to forecast the levels of debt instruments are described later in this chapter.

3.112 We typically use financial market expectations to derive relevant interest rates (for example, coupons on newly issued conventional gilts), while our inflation forecast is used for index-linked gilts and other index-linked debt. Flows associated with the Bank of England's Asset Purchase Facility (APF) and its own balance sheet similarly apply appropriate interest rates to the APF's loan liability and to the stocks of gilt, corporate bond and loan assets.

3.113 Given the large fiscal easing announced in this Budget, we have adopted a different approach to forecasting interest rates in this *EFO*. Our pre-measures forecast is conditioned on market interest rates from mid-February, but we have assumed somewhat higher interest rates in our post-measures forecast (as explained in Chapter 2). The effect is to add 0.26 percentage points on average to our post-measures Bank Rate forecast and 0.14 percentage points to our weighted-average gilt yield forecast. RPI inflation is also modestly higher on average over the forecast period as a result of the Budget measures.

[15] Our forecasting approach was explained in Box 4.4 of our March 2015 *EFO* and is discussed in the 'in depth' section of our website. A supplementary fiscal table on our website presents the different stocks, flows and effective interest rates that make up this forecast.

3.114 Debt interest spending is expected to fall in 2020-21 due to differences in RPI inflation. Interest payments then rise sharply in 2021-22 and by smaller margins across the rest of the forecast as the cost of financing new borrowing roughly equals the saving associated with rolling over previously issued debt at lower interest rates than those that prevailed when it was issued. Interest accrued in respect of public sector funded pensions also rises steadily, in line with the liabilities of these schemes. The APF continues to subtract from debt interest spending over the forecast, but by decreasing amounts each year as the gap between the average interest rate earned on its assets and Bank Rate paid on its liabilities narrows.

3.115 Table 3.22 shows the changes to our forecast since March 2019. On a pre-measures basis, these lower spending by progressively larger amounts reaching £8.8 billion in 2023-24:

- Lower RPI inflation reduces spending in all years but by decreasing amounts from 2020-21 onwards.
- Materially lower interest rate expectations – for both Bank Rate and gilt yields – reduce spending by progressively larger amounts. Lower Bank Rate reduces spending almost immediately, but the effect of lower gilt yields builds as more debt is issued.
- Financing the increase in cash borrowing in the pre-measures forecast increases spending slightly.

3.116 Budget measures have several effects on debt interest spending. Taken together these raise spending by £3.7 billion a year on average:

- The large fiscal easing announced in the Budget, combined with delays to some asset sales and the cancellation of others, adds progressively larger amounts to cash borrowing. Cumulatively this reaches £125 billion in 2024-25. Higher financing needs add £1.0 billion a year to debt interest spending by 2024-25.
- Our assumption of a higher path for Bank Rate and gilt yields than markets are currently expecting adds £2.2 billion a year on average, increasing the cost of central government debt and reducing the debt interest saving associated with the APF.
- Changes to RPI inflation associated with the Budget package and individual measures have uneven effects across the period, but add £0.4 billion a year on average.
- Other policies, such as changes to the terms on which local authorities can borrow from the Public Works Loan Board, have had small effects.

## Table 3.22: Key changes to debt interest since March

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Public sector debt interest | | | | | | |
| March 2019 forecast | 60.5 | 60.1 | 62.5 | 64.8 | 66.7 | |
| March 2020 forecast | 58.5 | 55.7 | 60.1 | 61.2 | 61.7 | 62.3 |
| Change | -2.0 | -4.4 | -2.5 | -3.7 | -5.0 | |
| *of which:* | | | | | | |
| Forecast changes | -2.3 | -7.0 | -6.9 | -8.0 | -8.8 | |
| Effect of Government decisions | 0.3 | 2.6 | 4.4 | 4.3 | 3.8 | 3.5 |
| Central government debt interest | | | | | | |
| March 2019 forecast | 51.1 | 48.7 | 49.3 | 49.2 | 49.7 | |
| March 2020 forecast | 49.0 | 44.7 | 47.6 | 46.5 | 45.9 | 45.2 |
| Change | -2.1 | -4.0 | -1.7 | -2.7 | -3.9 | |
| *of which:* | | | | | | |
| Forecast changes | -2.0 | -5.3 | -4.5 | -5.5 | -6.2 | |
| Interest rates | -0.3 | -2.2 | -3.2 | -4.3 | -5.2 | |
| Inflation | -1.9 | -3.4 | -1.7 | -1.6 | -1.4 | |
| Financing | 0.0 | 0.0 | 0.0 | 0.1 | 0.1 | |
| Other factors (including outturn) | 0.2 | 0.4 | 0.4 | 0.3 | 0.2 | |
| Effect of Government decisions | 0.0 | 1.3 | 2.8 | 2.8 | 2.3 | 2.2 |
| Interest rates | 0.0 | 0.5 | 0.9 | 1.1 | 1.3 | 1.5 |
| Inflation | -0.2 | 0.2 | 1.3 | 0.9 | 0.2 | -0.3 |
| Financing | 0.2 | 0.6 | 0.6 | 0.7 | 0.9 | 1.0 |
| Asset Purchase Facility | | | | | | |
| March 2019 forecast | -10.9 | -9.7 | -9.0 | -7.7 | -7.5 | |
| March 2020 forecast | -10.8 | -10.2 | -9.8 | -8.6 | -8.6 | -8.5 |
| Change | 0.1 | -0.4 | -0.8 | -0.9 | -1.1 | |
| *of which:* | | | | | | |
| Forecast changes | 0.1 | -1.4 | -2.1 | -2.2 | -2.3 | |
| Effect of Government decisions | 0.0 | 1.0 | 1.3 | 1.2 | 1.1 | 1.0 |
| Local authority and public corporation debt interest | | | | | | |
| March 2019 forecast | 20.2 | 21.2 | 22.2 | 23.3 | 24.4 | |
| March 2020 forecast | 20.3 | 21.2 | 22.2 | 23.3 | 24.4 | 25.6 |
| Change | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| *of which:* | | | | | | |
| Forecast changes | -0.3 | -0.3 | -0.3 | -0.3 | -0.3 | |
| Effect of Government decisions | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 |

### Scottish Government AME

3.117 Scottish Government expenditure is treated as AME, ostensibly because an increasing proportion of expenditure is self-financed from taxation and thus falls outside Treasury control. But the majority is funded from a (residual) block grant that is tightly linked to central government DELs via the Barnett formula. The Scottish Government announced its latest spending plans in February 2020, which we have used as the starting point to update our forecast. And we have incorporated the effects of a restatement of the block grant when compared with March 2019, which is discussed in Annex A, and the devolution of disability benefits, which shifts £3.0 billion a year on average from DWP welfare spending to Scottish Government current AME.

3.118 The largest effect on Scottish Government expenditure that adds to total spending rather than shifting it between lines is the Barnett consequential changes in the block grant as a result of the large increases in RDEL and CDEL plans announced in the Budget. We have treated these essentially DEL-like components of Scottish spending in the same way as the DEL increases, assuming a 5 per cent underspend relative to current spending and a 20 per cent underspend relative to capital spending. The net effect of the higher block grants and the underspend assumptions increases in Scottish Government current and capital expenditure by £3.7 billion and £1.4 billion respectively in 2024-25. This simple approach of treating the block grant changes like DEL changes will need to be revisited in our autumn forecast, in the light of the Spending Review and Scottish Government plans.

## Funded public sector pensions

3.119 The ONS brought funded public sector pension schemes into the public finances data in September 2019. We explained the implications of this, and our methodology for forecasting them, alongside the December restatement of our March 2019 forecast. As we set out, these schemes fall into three categories:

- Funded schemes with largely public sector members, notably the Local Government Pension Scheme, which covers 14,800 employers and has 5.8 million members.
- The Pension Protection Fund (PPF), which takes over the assets and liabilities of defined benefit schemes, largely from insolvent private sector firms. Such schemes are closed to new contributions after they have been taken into the PPF, while benefits paid out are also reduced.
- The National Employment Savings Trust (NEST), which facilitates auto-enrolment as part of the workplace pension reforms in the Pensions Act 2008.

3.120 Our receipts and spending forecasts focus on accrued changes to these entities. The largest elements are related to the schemes with public sector members, where actuarial concepts of scheme income and expenditure are recorded as interest receipts and spending. These flows are derived from balance sheet estimates and are relatively stable from year to year, but potential variability arises from schemes entering the PPF. Liquid assets held by all the funds net off public sector net debt, while their government bond holdings consolidate out (as they are treated as central government liabilities to another part of the public sector).

3.121 There has been little change to our forecasts for these schemes since our restated March 2019 forecast. We have drawn on more detailed information to forecast net asset transfers into the PPF, reducing spending in 2019-20 by £0.1 billion.

3.122 A potential upside risk to this forecast relates to the possible transfer of the Kodak Pension Plan 2 into the PPF. In its 2018-19 annual report, the PPF reported a provision of around £3 billion, much of which relates to the Kodak scheme, which is currently under assessment. The result of this assessment, and the timing of any subsequent transfer of assets and liabilities to the PPF is uncertain, so has not been reflected in our central forecast.

## Student loans

3.123 Student loans generate a mix of receipts, spending and financial transactions, all of which are discussed in this section. Changes to the statistical treatment of student loans have materially affected the public finances. Our restated March 2019 forecast discussed the impact of the new ONS 'partitioned loan approach' on PSNB and its components. Our net investment forecast was revised up by £11.5 billion on average compared to the previous treatment due to capital transfers from outlays and sales being recorded as spending.

3.124 Table 3.24 summarises the main changes relative to our restated March 2019 forecast:

- Modelling changes add progressively larger amounts to capital spending at outlays, reaching £1.3 billion in 2023-24. This largely reflects a higher proportion of new outlays being treated as spending, in part to reflect better the reduced likelihood of repayment by students taking out their second or subsequent Plan 2 loans.

- Upward revisions to student entrants that are eligible for loans adds £0.6 billion on average to capital spending. As Table 3.23 shows, this is split between revisions to entrants at higher education institutions (which represents higher entrant numbers overall) and to entrants at alternative providers that are now registered with the Office for Students (which is in essence a classification change[16]). Our forecast reflects a judgement that providers will increase acceptance rates in years where applications are likely to be affected by decline in the 18-year-old population. The extent to which they do so is uncertain, with upside surprises in the latest data suggesting a stronger response than we had previously assumed. Higher education institutions themselves expect student numbers to rise much faster than we do.[17] If student entrants were to rise 22 per cent over the next five years, in line with their collective predictions, rather than the 5 per cent we assume, capital spending in 2024-25 would be £1.8 billion higher (0.1 per cent of GDP) and public sector net debt would be £10.0 billion higher (0.4 per cent of GDP).

- Downward revisions to RPI inflation and Bank Rate have reduced modified interest receipts by £0.2 billion a year on average.

- We have reduced long-term productivity growth, resulting in long-term average earnings growth being 0.5 per cent a year lower than we assumed a year ago. This implies that a lower proportion of the loan outlay will ultimately be repaid, and therefore more written off, raising the forecast for capital spending at outlay by an average of £0.4 billion a year, but with no effect on total outlays in the forecast period.

[16] Being registered as 'Approved (fee cap)' means providers can charge maximum tuition fees of £9,250 per year whereas previously the maximum had been £6,125. Previously, outlays to students at designated alternative providers were modelled in aggregate rather than via student numbers and average loans. Unfortunately, given the large volume of modelling work undertaken by DfE's student loans team over the past year, it has not been possible to restate our previous forecast to be on a consistent basis and show only like-for-like changes.
[17] See, for example, the discussion in *The official forecast of student numbers that is so often wrong, it's nicknamed 'the hedgehog'*, Nick Hillman, HEPI blog, December 2019.

## Table 3.23: English-domiciled student entrants eligible for student loans

| | Thousand | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast[1] | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| English-domiciled | | | | | | | |
| March 2019 forecast | 330 | 334 | 328 | 328 | 332 | 336 | |
| March 2020 forecast | 344 | 360 | 362 | 364 | 366 | 371 | 381 |
| Change | 14 | 26 | 35 | 36 | 35 | 35 | |
| of which: | | | | | | | |
| Higher education institutions | 14 | 12 | 20 | 22 | 20 | 20 | |
| Approved (fee cap) | 0 | 14 | 14 | 15 | 15 | 15 | 15 |

[1] Academic years.

## Table 3.24: Key changes in student loans forecasts since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Capital spending (PSNI) (a) | | | | | | |
| Restated March 2019 forecast | 11.2 | 11.6 | 11.9 | 12.2 | 10.4 | |
| March 2020 forecast | 9.9 | 10.7 | 11.3 | 12.0 | 12.5 | 12.9 |
| Change | -1.3 | -0.9 | -0.6 | -0.2 | 2.1 | |
| *of which:* | | | | | | |
| Modelling changes | 0.0 | 0.5 | 1.0 | 1.3 | 1.3 | |
| Student numbers | 0.4 | 0.5 | 0.5 | 0.7 | 0.7 | |
| Economic determinants changes | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| Long term economic assumptions | 0.3 | 0.4 | 0.4 | 0.4 | 0.5 | |
| Government decisions | -2.1 | -2.3 | -2.5 | -2.6 | -0.4 | -0.4 |
| Modified interest (receipt) (b) | | | | | | |
| Restated March 2019 forecast | 2.7 | 2.9 | 3.4 | 3.9 | 4.5 | |
| March 2020 forecast | 2.8 | 2.9 | 3.2 | 3.8 | 4.4 | 4.8 |
| Change | 0.1 | 0.0 | -0.2 | -0.2 | 0.0 | |
| PSNB (c=a-b) | | | | | | |
| Restated March 2019 forecast | 8.5 | 8.7 | 8.5 | 8.3 | 5.9 | |
| March 2020 forecast | 7.1 | 7.7 | 8.1 | 8.2 | 8.1 | 8.1 |
| Change | -1.4 | -1.0 | -0.4 | -0.1 | 2.1 | |
| Financial transactions (d) | | | | | | |
| Restated March 2019 forecast | 5.9 | 6.5 | 7.1 | 7.8 | 13.8 | |
| March 2020 forecast | 8.8 | 8.8 | 9.1 | 9.7 | 10.5 | 11.0 |
| Change | 2.9 | 2.3 | 2.0 | 1.9 | -3.3 | |
| Public sector net cash requirement (c+d) | | | | | | |
| Restated March 2019 forecast | 14.4 | 15.2 | 15.6 | 16.1 | 19.7 | |
| March 2020 forecast | 15.9 | 16.6 | 17.2 | 18.0 | 18.6 | 19.1 |
| Change | 1.5 | 1.4 | 1.6 | 1.8 | -1.1 | |
| *Memo: Total cash outlays (a+d)* | *18.7* | *19.5* | *20.4* | *21.7* | *23.0* | *23.9* |

3.125 Several policies affect our student loans forecasts. Most have modest and partly offsetting effects: freezing tuition fees next year, not providing part-time maintenance loans and providing greater support for nursing and related courses. The largest effect comes from the cancellation of Plan 1 student loan sales. In our pre-measures forecast, the sales planned for 2019-20 to 2022-23 were expected to add on average £2.1 billion a year to capital spending over that period and to reduce modified interest by £0.3 billion a year by 2024-25. Cancelling the sales reverses those effects, as discussed in the asset sales section below.

3.126 In May 2019, the Government confirmed student finance eligibility for EU nationals in the 2020-21 academic year.[18] In the absence of a specified policy beyond this, we have assumed that EU-domiciled student entrants will be stable at 28,000 a year. EU-domiciled students thus account for 7 per cent of loan-eligible student entrants in our forecast. If eligibility were to be tightened or removed in future, this would lower outlays and spending.

### Net expenditure transfers to EU institutions

3.127 In our forecasts since November 2016, we have taken a fiscally neutral approach to our post-Brexit spending forecast, assuming that when the UK leaves the EU any reductions in net expenditure transfers to Brussels would be fully recycled into extra spending.

3.128 In effect, this meant that we were compiling the forecast for net expenditure transfers to the EU as though the UK were not leaving the EU, and were incorporating an assumption that those funds (in effect 'DEL in waiting') would eventually be spent after the UK's withdrawal (rather than reducing borrowing). This assumption has been borne out by the higher departmental spending set out in this Budget, so we have now removed the 'DEL in waiting' component of our AME forecast (see Box 3.5). This section therefore focuses on changes to our estimate of the cost of the financial settlement.

3.129 In our March 2019 forecast, we estimated that the financial settlement would cost £37.8 billion, assuming that the UK would leave the EU on 29 March 2019. The subsequent delay to 31 January 2020 has reduced the size of the financial settlement, but this has made no difference to overall payments to the EU, as it merely extended the period during which contributions were made as an EU member state. On the basis of a 31 January 2020 exit, our March 2019 estimate of the financial settlement would have been £30.4 billion.

3.130 We have raised the cost of the financial settlement to £32.9 billion, £2.5 billion higher than in March 2019. Only some of these flows are recorded in AME. These include:

- Net contributions as though the UK remained a member until December 2020.
- Payments of the *reste à liquider* (RAL), which represents outstanding commitments at the end of the 2014-20 EU budget period and which we expect to continue until 2028.
- Non-financial net liabilities, including pension payments and some other EU schemes, for which some payments are expected to continue until 2064.

[18] Department for Education, *EU student funding continued for 2020/21*, 28 May 2019.

3.131 Table 3.25 breaks down the financial settlement flows recorded within and outside AME. Total payments recorded within AME amount to £47.8 billion (of which £10.9 billion lie beyond our present forecast horizon). These are partially offset by £15.0 billion of net receipts not recorded in AME (£2.8 billion beyond the forecast horizon). The latter include:

- public and private sector receipts during the transition period and from the RAL, which reduce the cost of the settlement for the UK as a whole but not for the Government;
- the remittance of customs duties collected on behalf of the EU until December 2020, net of the cost of collection; and
- repayments of equity in the European Investment Bank and European Central Bank, which are financial transactions and therefore affect debt but not expenditure.

## Table 3.25: Financial settlement components by time period

| | £ billion | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Forecast | | | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 | 2025-64 | Total |
| March 2020 forecast | 0.6 | 8.0 | 6.8 | 5.2 | 2.9 | 1.2 | 8.2 | 32.9 |
| *of which:* | | | | | | | | |
| In AME | 2.0 | 9.2 | 10.6 | 8.3 | 4.7 | 2.2 | 10.9 | 47.8 |
| Not in AME | -1.3 | -1.2 | -3.9 | -3.0 | -1.8 | -1.0 | -2.8 | -15.0 |

3.132 On a like-for-like basis, we have revised up the AME component of the financial settlement relative to March 2019 by £0.9 billion. This reflects:

- A stronger sterling-euro exchange rate that reduces the cost by £2.5 billion, since the UK's financial settlement liabilities are denominated in euros.
- An adjustment to the profile of settlement payments to reflect the fact that payments will accrue twice a year after December 2020, when notification of the liability is given to the UK. This affects when payments will hit spending rather than the overall cost of the settlement. This lowers spending in 2020-21 and increases it in subsequent years.
- Slower than forecast implementation of the EU's 2014-20 multiannual financial framework, which pushes more expenditure into the *reste à liquider* (RAL). This increases the financial settlement by £1.2 billion, but has lowered our contributions while a member state.
- The monthly pattern of contributions in 2020, which has included higher-than-expected contributions in January but a lower-than-expected draw-forward for the whole of the first quarter. This shifts payments into 2020-21, but reduces the overall size of the payments within the financial settlement by £0.3 billion.
- Updated European Commission estimates of the cost of pension liabilities, which have added £2.6 billion (mostly beyond the forecast horizon).

3.133 We have revised the non-AME component up by £1.6 billion. This is due to a stronger sterling-euro exchange rate and an updated monthly pattern of receipts, which reduced customs duties remittances and private sector receipts falling into the financial settlement.

## Table 3.26: Sources of change in the financial settlement since March 2019

| | £ billion | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Forecast | | | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 | 2025-64 | Total |
| Like-for-like changes in AME since March 2019 | -1.8 | -1.2 | 0.3 | 0.6 | 0.6 | 0.2 | 2.3 | 0.9 |
| *of which:* | | | | | | | | |
| Sterling-euro exchange rate | 0.0 | -0.2 | -0.8 | -0.6 | -0.3 | -0.1 | -0.5 | -2.5 |
| Payments accrue twice a year | 0.0 | -2.5 | 0.5 | 0.9 | 0.6 | 0.2 | 0.3 | 0.0 |
| More spending in the reste a liquider | 0.0 | 0.0 | 0.4 | 0.2 | 0.3 | 0.1 | 0.2 | 1.2 |
| Monthly pattern of 2020 contributions | -1.8 | 1.5 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | -0.3 |
| Higher pensions liabilities | 0.0 | 0.0 | 0.1 | 0.1 | 0.0 | 0.0 | 2.4 | 2.6 |
| Like-for-like changes not in AME since March 2019 | 0.8 | 1.3 | 0.0 | -0.1 | -0.1 | 0.0 | -0.3 | 1.6 |
| *of which:* | | | | | | | | |
| Sterling-euro exchange rate | 0.0 | 0.1 | 0.3 | 0.2 | 0.1 | 0.1 | 0.2 | 1.0 |
| Monthly pattern of receipts | 0.8 | 1.2 | -0.3 | -0.3 | -0.2 | -0.1 | -0.4 | 0.6 |

### Box 3.5: Spending the direct fiscal savings from Brexit

In our November 2016 *EFO*, we set out broad-brush assumptions regarding the UK's prospective exit from the EU. These included two fiscally neutral holding assumptions, related to the UK's direct fiscal interactions with the EU – namely the transfers to EU institutions that feature in AME spending and the customs duties collected on behalf of the EU. Specifically, we assumed that net expenditure transfers to EU institutions – after factoring in the cost of the financial settlement – would be fully recycled into substitute UK spending. These transfers were labelled as 'Assumed spending in lieu of EU transfers' in AME, but have in effect been 'DEL in waiting'. Customs duties were treated in the same way, but on a net rather than a gross basis.

We do not typically anticipate Government policy in this way, but it quickly made commitments in respect of farming support, industrial strategy and science programmes that meant that if we had not done so, our central forecast would have been inconsistent with the intended path of public spending. Now that the UK has left the EU and the Government has set out the path of departmental spending over the next five years, we can remove the assumption that the direct fiscal savings from Brexit will be spent – there is no more 'DEL in waiting' as it is now in DEL.

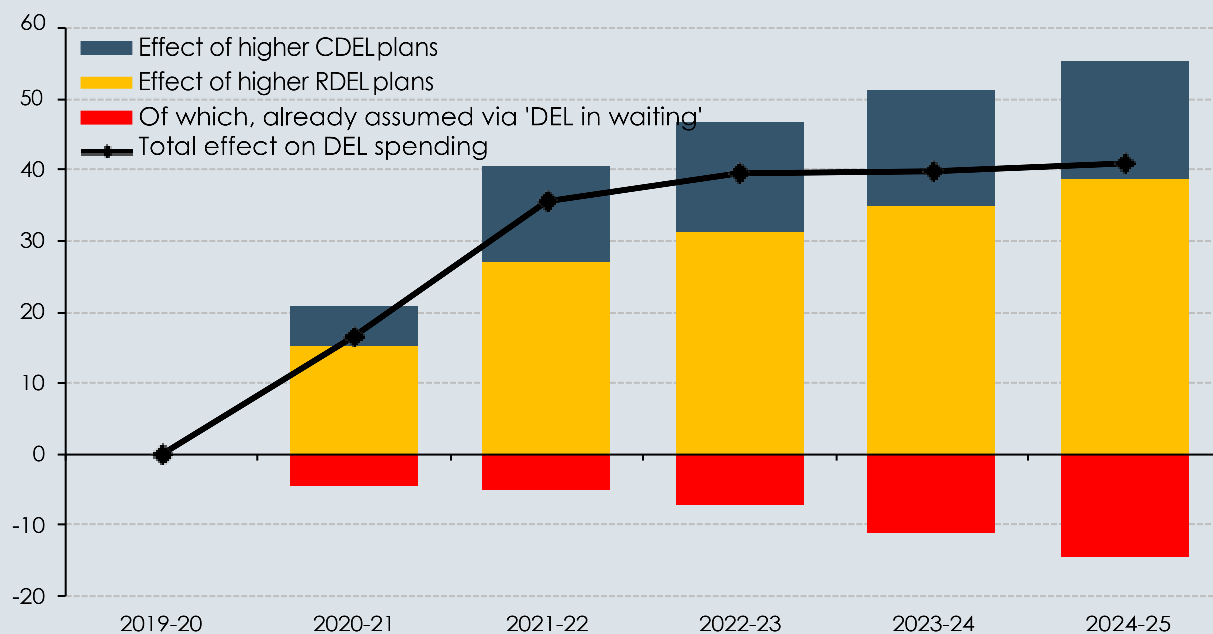
As the Government has chosen to increase DEL spending by more than the implied AME savings and retained customs duty receipts, it is moot – from the point of view of the overall public finances – whether the Government will actually fully replace all the previous EU spending programmes. We have therefore not attempted to map the individual spending lines.

Table C shows how we moved from our pre-measures forecast containing 'DEL in waiting' within AME to a post-measures forecast with that assumption removed. 'DEL in waiting' was the sum of customs duties retained from January 2021 and the difference between our 'no-referendum counterfactual' view of EU transfers and the financial settlement. This increased from £4.3 billion in 2020-21 to £14.6 billion in 2024-25. After our underspend assumptions, the Government's new DEL spending plans raise RDEL and CDEL spending in 2024-25 by £38.9 billion and £16.7 billion respectively. This means £40.9 of the £55.5 billion increase in DEL spending in 2024-25 feeds through to higher total managed expenditure and therefore to borrowing (Chart C).

## Table C: DEL spending and use of the direct fiscal savings from Brexit

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Pre-measures DEL spending | | | | | | |
| Total including 'DEL in waiting' | 376.2 | 394.4 | 408.0 | 423.0 | 443.5 | 462.4 |
| *of which:* | | | | | | |
| RDEL spending | 316.3 | 324.6 | 334.3 | 344.7 | 356.8 | 369.7 |
| CDEL spending | 59.9 | 65.5 | 68.8 | 71.2 | 75.4 | 78.1 |
| 'DEL in waiting' | 0.0 | 4.3 | 5.0 | 7.1 | 11.3 | 14.6 |
| In lieu of EU transfers | 0.0 | 3.5 | 1.7 | 3.8 | 7.9 | 11.3 |
| Retained customs duties | 0.0 | 0.8 | 3.3 | 3.3 | 3.3 | 3.3 |
| Post-measures DEL spending | | | | | | |
| Total | 376.2 | 411.0 | 443.5 | 462.5 | 483.3 | 503.4 |
| *of which:* | | | | | | |
| RDEL spending | 316.3 | 339.8 | 361.3 | 375.9 | 391.8 | 408.6 |
| CDEL spending | 59.9 | 71.2 | 82.2 | 86.6 | 91.5 | 94.8 |
| 'DEL in waiting' | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| In lieu of EU transfers | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Retained customs duties | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Difference | | | | | | |
| Total | 0.0 | 16.6 | 35.5 | 39.5 | 39.8 | 40.9 |
| *of which:* | | | | | | |
| RDEL spending | 0.0 | 15.2 | 27.0 | 31.2 | 34.9 | 38.9 |
| CDEL spending | 0.0 | 5.7 | 13.4 | 15.4 | 16.1 | 16.7 |
| 'DEL in waiting' | 0.0 | -4.3 | -5.0 | -7.1 | -11.3 | -14.6 |
| In lieu of EU transfers | 0.0 | -3.5 | -1.7 | -3.8 | -7.9 | -11.3 |
| Retained customs duties | 0.0 | -0.8 | -3.3 | -3.3 | -3.3 | -3.3 |

Chart C: DEL-in-waiting versus new DEL spending plans




Source: OBR

## Public service pensions

3.134 Our net public service pensions forecast covers gross expenditure on pensions in payment, less employer and employee contributions received. (The corresponding spending by departments on employer contributions is included in RDEL.) The forecast includes central government pay-as-you-go schemes and locally administered police and firefighters' schemes.[19] A breakdown of spending and income for the major schemes we cover can be found in the supplementary tables on our website.

3.135 Table 3.27 breaks down the changes to our forecast since March 2019. Reduced scheme expenditure and higher scheme income have combined to lower net spending by increasing amounts, reaching £7.0 billion in 2023-24. The main changes relate to:

- Significantly higher RDEL spending, reflecting last year's Spending Round settlement and the further increases announced in the Budget, raises scheme income by increasing amounts. Full detail of how the higher RDEL will be allocated across departments, and therefore the precise amounts by which individual schemes' incomes will rise, will not be known until this year's Spending Review settlements. In the meantime we estimate that the higher RDEL will add £4.3 billion a year to total scheme income by 2024-25. This reduces net public service pension spending. The effect of the overall fiscal easing on CPI inflation has further modest implications for scheme expenditure.

[19] The police and firefighters' pension schemes are administered at a local level, but pensions in payment are funded from AME, along with other public service pension schemes. They are therefore included in our pensions forecast.

- Slower pre-measures growth in expenditure, reflecting lower forecast CPI inflation and the declining average age of teachers' pension scheme members. Updated retirement assumptions in the NHS pension scheme offset some of this decrease early in the forecast and augment it in later years. These pre-measures changes reduce expenditure by increasing amounts, reaching £1.4 billion in 2023-24.

- Higher pre-measures contributions, which thanks to stronger paybill growth have boosted pension scheme income. The largest effect comes from the teachers' pension scheme. Higher contribution rates applied in several schemes from 2019-20 means that faster paybill growth boosts income proportionately more than previously.

3.136 Several other policy measures have smaller effects. Raising the annual allowance taper will reduce use of 'scheme pays' by public service pension scheme members. But scheme pays costs for the NHS scheme in respect of 2019-20 will be higher thanks to the Secretary of State for Health and Social Care's announcement that clinicians' annual allowance charges in that year will be paid by his department not the scheme members. Setting up an unfunded pension scheme for Bradford & Bingley and Northern Rock Asset Management scheme members adds a little to total scheme expenditure from 2023-24 onwards.

## Table 3.27: Key changes to public service pensions since March 2019

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Net public service pensions | | | | | | |
| March 2019 forecast | 6.7 | 6.4 | 7.3 | 7.9 | 8.2 | |
| March 2020 forecast | 6.9 | 4.2 | 2.9 | 2.0 | 1.2 | 0.3 |
| Change | 0.2 | -2.2 | -4.3 | -5.9 | -7.0 | |
| *of which:* | | | | | | |
| Forecast changes | 0.2 | -0.5 | -1.3 | -2.1 | -2.8 | |
| Effects of Government decisions | 0.0 | -1.7 | -3.0 | -3.8 | -4.2 | -4.6 |
| Expenditure | | | | | | |
| March 2019 forecast | 44.4 | 46.4 | 48.6 | 50.4 | 52.4 | |
| March 2020 forecast | 44.7 | 46.2 | 47.9 | 49.1 | 50.8 | 52.4 |
| Change | 0.2 | -0.2 | -0.7 | -1.3 | -1.6 | |
| *of which:* | | | | | | |
| Forecast changes | 0.2 | -0.2 | -0.7 | -1.1 | -1.4 | |
| Teachers' pension scheme | -0.2 | -0.3 | -0.3 | -0.4 | -0.5 | |
| NHS pension scheme | 0.4 | 0.3 | 0.3 | -0.2 | -0.6 | |
| Pre-measures CPI inflation | 0.0 | -0.1 | -0.4 | -0.2 | -0.2 | |
| Other | 0.1 | -0.1 | -0.3 | -0.3 | -0.2 | |
| Effect of Government decisions | 0.0 | 0.0 | 0.0 | -0.3 | -0.2 | -0.2 |
| Income | | | | | | |
| March 2019 forecast | -37.7 | -40.0 | -41.3 | -42.6 | -44.2 | |
| March 2020 forecast | -37.8 | -42.0 | -44.9 | -47.2 | -49.6 | -52.1 |
| Change | 0.0 | -2.0 | -3.6 | -4.6 | -5.4 | |
| *of which:* | | | | | | |
| Forecast changes | 0.0 | -0.3 | -0.6 | -1.1 | -1.4 | |
| Teachers' pension scheme | 0.0 | -0.1 | -0.3 | -0.5 | -0.8 | |
| Other | 0.0 | -0.2 | -0.3 | -0.6 | -0.6 | |
| Effect of Government decisions | 0.0 | -1.7 | -3.0 | -3.5 | -4.0 | -4.3 |

## Depreciation

3.137 We have revised up public sector depreciation by £0.6 billion a year from 2020-21 onwards. Our pre-measures forecast reflects fuller data on public sector capital stocks and the associated trends in depreciation rates than were available when producing our restated March 2019 forecast. We have also incorporated the latest splits of capital spending across central government, local authorities and public corporations, which show less spending by central government but more by local authorities and public corporations. Together, these changes have increased depreciation in the early years of the forecast, and decreased it later. The large increase in capital spending in the Budget adds progressively larger amounts to depreciation, reaching £1.0 billion in 2024-25. The precise composition of this spending is not yet known, so we have largely drawn on recent data to estimate this effect.

### Table 3.28: Key changes to public sector depreciation since restated March 2019

| | £ billion | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Restated March 2019 forecast | 48.7 | 49.8 | 51.6 | 53.5 | 55.5 | 57.5 | |
| March 2020 forecast | 48.8 | 49.9 | 52.2 | 54.0 | 56.0 | 58.1 | 60.3 |
| Change | 0.1 | 0.1 | 0.6 | 0.5 | 0.6 | 0.6 | |
| *of which:* | | | | | | | |
| Forecast changes | 0.1 | 0.1 | 0.6 | 0.3 | 0.0 | -0.2 | |
| Effect of Government decisions | 0.0 | 0.0 | 0.1 | 0.2 | 0.5 | 0.8 | 1.0 |

## Other AME

3.138 The main changes to other AME spending items include:

- Spending on company tax credits is up by an average of £2.6 billion a year from 2019-20 onwards, almost entirely due to higher spending on R&D tax credits. Just £0.2 billion of this reflects the Budget increase the R&D expenditure credit rate from 12 to 13 per cent. Most reflects evidence of large increases in use of the small firms' element. It appears that this is at least partly due to abuse of the generous payable credits. We would have revised spending up by more were it not for the reintroduction from April 2020 of a cap on scheme use related to each firm's PAYE liability.

- Uneven revisions to spending associated with tax litigation payouts, based on updated information from HMRC. Relative to March 2019 this shifts spending into later years, while the overall cost over five years is slightly higher due to new cases.

- Some elements of our spending forecast are largely neutral for borrowing, because they are directly offset in receipts. These include environmental levies (which are up in the near term) and VAT refunds to central and local government (which are up thanks to the Budget spending announcements). These are detailed in the relevant receipts sections.

- Spending by the Land Registry and Companies House has been switched from AME to DEL from 2020-21 onwards, raising DEL spending and lowering other AME spending by £0.4 billion a year.

## Deficit aggregates

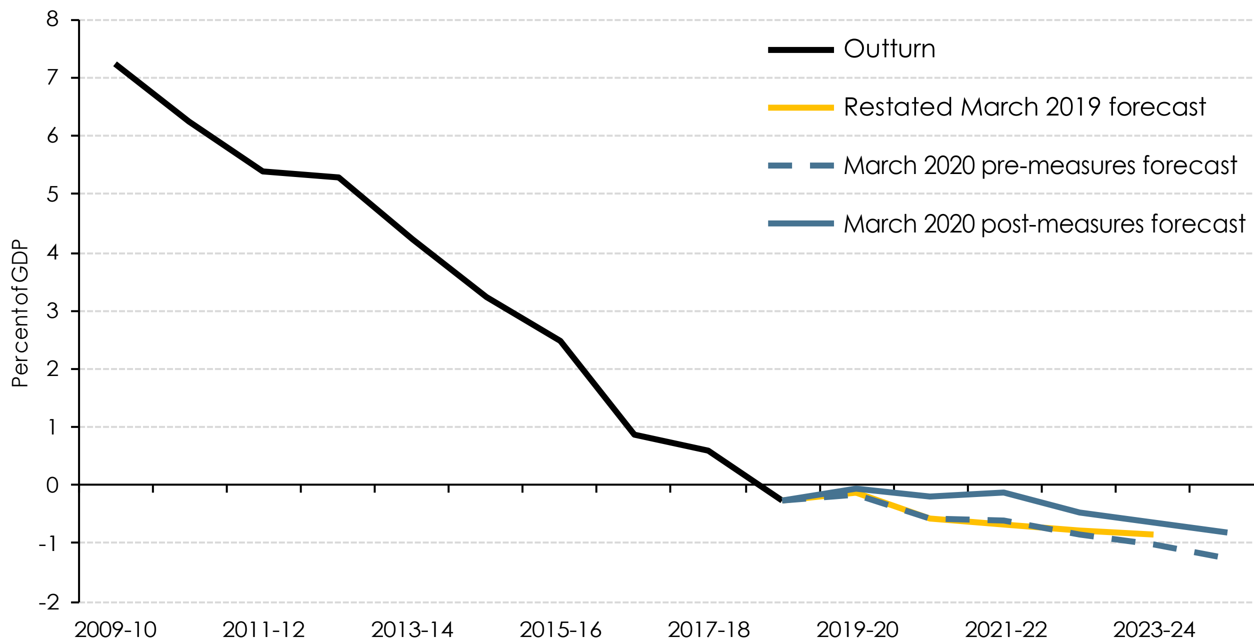
3.139 Our central forecast for the key measures of the Government's budget deficit incorporate the forecasts for receipts and expenditure set out in the previous sections of this chapter. In this section we explain the changes in the following aggregate measures of the deficit:

- Public sector net borrowing (PSNB): the difference between total public sector receipts and expenditure on an accrued basis each year – the widest measure of borrowing.
- Cyclically adjusted net borrowing: PSNB adjusted to reflect the estimated impact of the economic cycle. It is a measure of underlying or 'structural' net borrowing, in other words the borrowing we would expect to see if the output gap were zero.
- The current budget deficit: the difference between receipts and public sector current expenditure each year. In other words, public sector net borrowing excluding borrowing to finance investment that boosts the public sector capital stock.
- The cyclically adjusted current budget deficit: the current budget that we would expect to see if the output gap was zero.
- Public sector net investment (PSNI): the difference between gross capital spending and depreciation each year. In broad terms, the net increase in the capital stock each year.

### Current budget balance

3.140 The latest ONS data record a current budget surplus of 0.3 per cent of GDP in 2018-19 – the first surplus since 2001-02, following nine years of deficit reduction from the peak of 7.2 per cent of GDP reached during the financial crisis and recession. Our restated March 2019 forecast predicted that the surplus would narrow in 2019-20, before widening again to average 0.7 per cent of GDP between 2020-21 and 2023-24. Absent the effect of policy measures, we would have made only small changes to this forecast. The combined effect of measures announced in the Budget, the new migration regime and the higher path for the National Living Wage reduce the surplus by 0.4 per cent of GDP on average.

## Chart 3.5: Current budget deficit




Source: ONS, OBR

### Underlying forecast revisions

3.141 On average between 2020-21 and 2023-24, underlying revisions increase the surplus by £1.5 billion a year on average (less than 0.1 per cent of GDP), reflecting several factors:

- Total receipts have been revised down by £3.0 billion a year on average, despite an upward revision of £4.9 billion in 2019-20 (much of which reflects one-off factors). The deterioration is more than explained by changes in our economy forecast, in particular the weaker outlook for earnings growth and hence household spending.
- Debt interest spending has been revised down by £7.4 billion a year on average. This reflects lower Bank Rate expectations (which lower spending almost immediately), lower gilt yields (the effect of which builds up as more new debt is issued) and lower RPI inflation (which reduces spending in all years, but by decreasing amounts).
- Other current spending has been revised up by £2.8 billion a year on average, mostly in the near term. Almost all of this reflects higher spending on R&D tax credits, following large increases in use of the small firms' element in recent years. Welfare spending has also been revised up, in particular on incapacity benefits.

### Government decisions

3.142 Government decisions reduce the current surplus by £10.2 billion on average between 2020-21 and 2024-25 (0.4 per cent of GDP). This includes both the direct impact of Budget tax and spending measures and the indirect effect of those measures, plus the migration and NLW announcements, on the economy. The direct impact arises from:

- Large increases in current departmental spending limits (RDEL) that rise from £15.2 billion in 2020-21 to £38.9 in 2024-25 (reflecting higher plans and our assumptions about underspending relative to them). This is partly offset by some of that in effect confirming the 'DEL in waiting' included in our previous post-referendum forecasts, which assumed that direct fiscal savings from Brexit (i.e. contributions not paid plus customs duties retained) would be fully recycled into higher UK government spending. As that has now happened, removing the 'DEL in waiting' assumption lowers current spending by £4.3 billion in 2020-21 rising to £14.6 billion in 2024-25, with the rising profile reflecting the declining cost of the divorce bill over those years.

- Other spending measures (both on and off the Treasury's scorecard) raise borrowing by £2.2 billion a year on average. This is more than explained by the Government's decision to raise the current spending envelope of the Scottish Government by £3.4 billion a year on average between 2021-22 and 2024-25 (in line with higher RDEL).

- Receipts measures (both on and off the scorecard) reduce borrowing by an average of £6.4 billion a year. This is mostly explained by the decision to cancel the April 2020 cut in the main rate of corporation tax from 19 to 17 per cent, which raises £6.4 billion a year on average. Raising the National Insurance 'primary threshold' to £9,500 in 2020-21 costs £2.3 billion a year on average, while restricting eligibility for 'red diesel' raises £1.8 billion a year from 2022-23 onwards.

3.143 The indirect effects of the Government's decisions reduce borrowing across the forecast:

- Indirect effects of Budget tax and spending measures reduce borrowing by £6.6 billion a year on average. The significant overall easing in fiscal policy delivers a cyclical boost to the economy that lifts tax receipts via higher earnings and consumption in particular. Its temporary effect on inflation leads to permanently higher nominal GDP and tax bases. The boost to receipts therefore peaks at £11.5 billion in 2022-23 but remains at £8.9 billion in 2024-25. Higher departmental spending lifts public service pension contributions, reducing the medium-term net cost of these schemes. Conversely, the higher borrowing, higher interest rates and temporarily higher RPI inflation combine to raise debt interest spending.

- Raising the National Living Wage to reach two-thirds of median earnings by October 2024 reduces current borrowing overall. As Box 2.5 describes, the effects of this on current borrowing – which reach £1.2 billion in 2024-25 – include the boost to income tax and NICs receipts and the reduction in welfare spending associated with higher pay. These are partly offset by the effect of lower profits on corporation tax receipts and modestly higher inflation on debt interest spending.

- The new migration regime raises current borrowing by amounts rising to £1.0 billion in 2024-25. As Box 3.6 sets out, we have assumed that the new regime will leave the population in that year 0.4 smaller than it would otherwise have been, but because lower migration will be concentrated among those who would have been lower paid, the effect on nominal GDP is smaller at 0.3 per cent. The main effects of this are to reduce tax receipts by £1.5 billion and welfare spending by £0.5 billion.

## Table 3.29: Changes to the current budget deficit since March 2019

| | £ billion | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Restated March 2019 forecast | -5.4 | -2.5 | -13.3 | -15.7 | -18.6 | -21.1 | |
| March 2020 forecast | -5.8 | -1.7 | -4.9 | -2.7 | -11.7 | -16.7 | -21.2 |
| Change | -0.4 | 0.8 | 8.4 | 13.0 | 6.9 | 4.4 | |
| Underlying revisions | -0.4 | -1.2 | 0.1 | 0.8 | -2.1 | -4.7 | |
| *of which:* | | | | | | | |
| Receipts[1] | -3.3 | -4.9 | 1.0 | 3.5 | 4.1 | 3.5 | |
| Debt interest | 0.5 | -2.0 | -6.7 | -6.6 | -7.7 | -8.5 | |
| Other spending[1] | 2.4 | 5.7 | 5.8 | 3.8 | 1.4 | 0.3 | |
| Total effect of Government decisions[2] | | 2.0 | 8.3 | 12.3 | 9.0 | 9.0 | 12.5 |
| *of which:* | | | | | | | |
| Current departmental spending[2] | | 2.9 | 15.2 | 27.0 | 31.2 | 34.9 | 38.9 |
| Use of direct Brexit fiscal savings | | 0.0 | -4.3 | -5.0 | -7.1 | -11.3 | -14.6 |
| Receipts measures[3] | | -1.0 | -2.0 | -4.6 | -8.0 | -8.6 | -8.5 |
| Other spending measures[3] | | 0.1 | 2.7 | 1.7 | 2.1 | 1.6 | 2.9 |
| Indirect effects of Government decisions | | 0.0 | -3.3 | -6.9 | -9.2 | -7.6 | -6.2 |
| *of which:* | | | | | | | |
| Due to tax and spending measures | | 0.0 | -3.3 | -6.9 | -9.2 | -7.5 | -6.0 |
| Raising the National Living Wage | | 0.0 | 0.0 | -0.3 | -0.6 | -0.9 | -1.2 |
| New migration regime | | 0.0 | 0.0 | 0.3 | 0.5 | 0.8 | 1.0 |
| *Memo: March 2020 pre-measures forecast* | *-5.8* | *-3.7* | *-13.2* | *-14.9* | *-20.8* | *-25.8* | *-33.7* |

[1] Excludes the impact of customs duties switch, which raises receipts and current spending by the same amount.
[2] The change in 2024-25 is relative to a baseline that assumes DEL would otherwise have remained constant as a share of GDP.
[3] Includes both scorecard and non-scorecard measures. See Annex A for more information.
Note: this table uses the convention that a negative figure means a reduction in PSNB. i.e. an increase in receipts or a reduction in spending will have a negative effect on PSNB.

### Cyclically adjusted current budget deficit

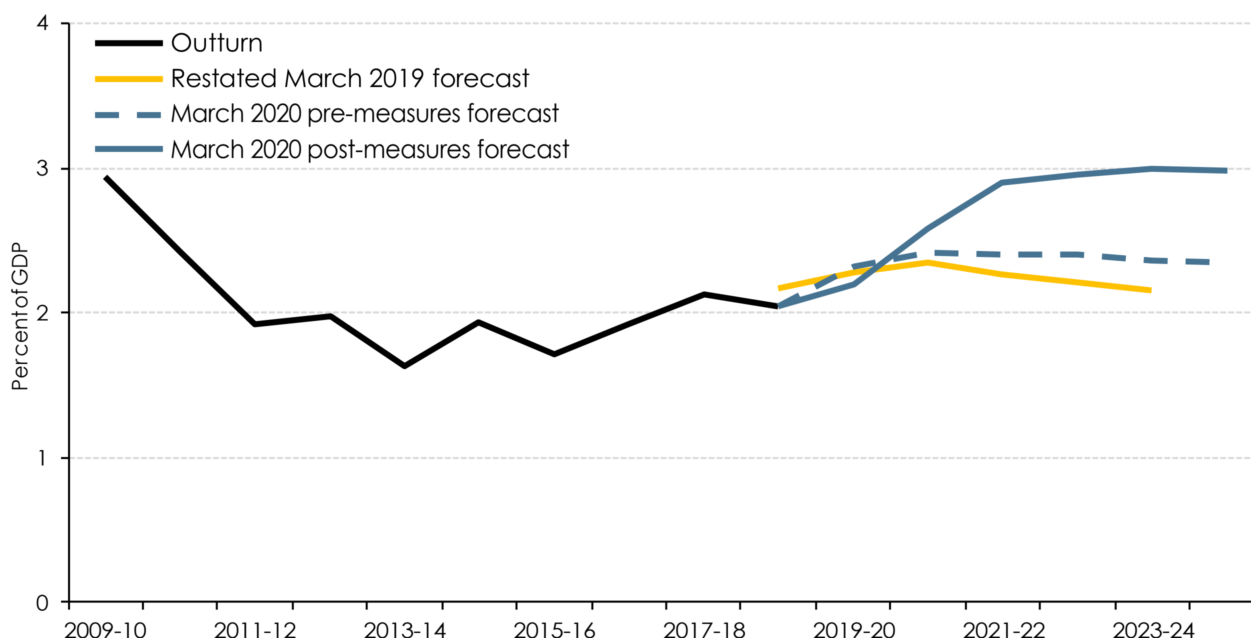
3.144 On a pre-measures basis, our forecast for the cyclically adjusted current budget is very similar to that for the headline balance. But our post-measures forecasts differ. The direct costs of Budget measures and the indirect effects of the new migration regime and NLW are structural, so have the same effect on cyclically adjusted borrowing as they do on headline borrowing. The indirect effects of the Budget package on the economy are entirely cyclical when viewed in terms of real GDP, so have little effect on cyclically adjusted borrowing. But because temporarily higher inflation leads to permanently higher nominal GDP, the Budget package does have a modest positive effect on the cyclically adjusted surplus. Taken together, these effects leave cyclically adjusted current borrowing close to balance between 2019-20 and 2022-23, before the surplus rises to 0.8 per cent of GDP in 2024-25.

## Public sector net investment

3.145 Public sector net investment (PSNI) almost halved as a share of GDP between 2009-10 and 2013-14, before rising slightly to average 1.9 per cent of GDP between 2014-15 and 2018-19. In our restated March 2019 forecast, we expected PSNI to average around 2.2 per cent of GDP. On a pre-measures basis, we have revised that up to around 2.4 per cent

of GDP. The Budget has placed capital spending on a significantly higher path, with PSNI rising to 2.9 per cent of GDP by 2021-22 and staying at 3.0 per cent thereafter.

## Chart 3.6: Public sector net investment




Source: ONS, OBR

### Underlying forecast revisions

3.146 Underlying revisions increase PSNI by progressively more across the forecast period – rising from £1.6 billion in 2019-20 to £6.2 billion in 2023-24 (Table 3.30):

- Roughly two thirds of this change reflects higher capital spending by local authorities and public corporations. In particular we have revised up borrowing-financed spending by English local authorities, which has risen rapidly in recent years.
- Much of the rest is explained by student loans. Under the new accounting treatment, loan outlays that are not expected to be repaid are treated as capital transfers that add to PSNI. Several factors have led us to revise up our forecast for these capital transfers, the largest of which relates to the proportion of each new loan treated as spending.

### Government decisions

3.147 Government decisions raise PSNI by £4.0 billion in 2020-21, then by £14.5 billion a year on average between 2021-22 and 2024-25. Table 3.30 shows that:

- Significant increases in departmental capital spending limits (CDEL) raise spending by amounts rising from £5.7 billion in 2020-21 to £16.7 billion in 2024-25. These amounts would have been higher still had we not assumed that 20 per cent of the increase in capital spending announced by the Treasury will go unspent – reflecting evidence of past difficulties in ramping up capital spending quickly (Box 3.2).

- Other spending measures reduce PSNI between 2019-20 and 2022-23, then raise it modestly in 2023-24 and 2024-25. The initial declines reflect the Government's decision not to sell any more tranches of student loans. As these sales raise less than the value of the loans recorded in the public finances, a capital transfer from government to private sector equal to that discount is recorded at the point of sale. Cancelling the sales removes around £2 billion a year of spending from 2019-20 to 2022-23. Scottish Government capital spending has been raised due to higher CDEL.

- These measures affect gross capital spending. To the extent that they add to the public capital stock, they have indirect effects on depreciation costs. These broadly follow the path of the cumulative rise in CDEL spending, raising depreciation and reducing PSNI by progressively larger amounts that reach £1.0 billion in 2024-25.

## Table 3.30: Changes to public sector net investment since March 2019

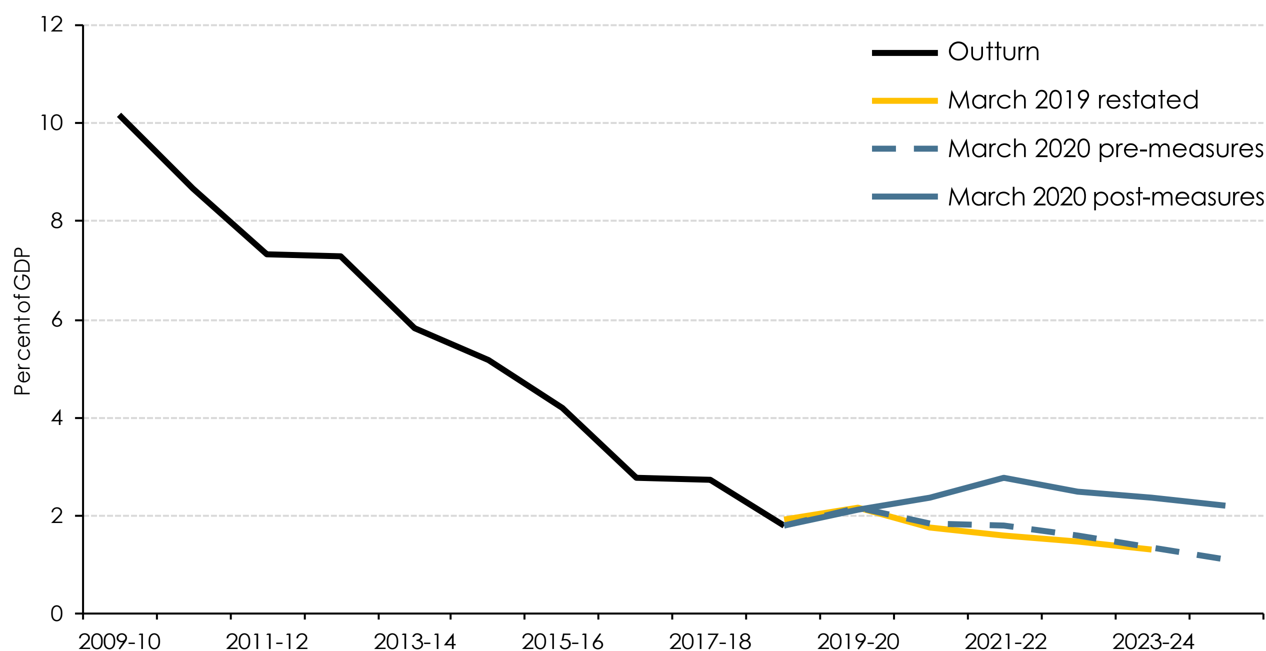
| | £ billion | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Restated March 2019 forecast | 46.4 | 50.2 | 53.6 | 53.3 | 54.1 | 54.4 | |
| March 2020 forecast | 44.3 | 49.1 | 59.7 | 69.3 | 73.2 | 77.0 | 79.1 |
| Change | -2.1 | -1.0 | 6.2 | 16.1 | 19.1 | 22.6 | |
| Underlying revisions to spending | -2.1 | 1.6 | 2.1 | 4.3 | 5.7 | 6.2 | |
| *of which:* | | | | | | | |
| LA and PC capital expenditure | -0.7 | 2.3 | 2.3 | 2.5 | 3.3 | 3.4 | |
| Student loans | 0.0 | 0.7 | 1.3 | 1.9 | 2.4 | 2.5 | |
| Other spending | -1.5 | -1.4 | -1.5 | -0.1 | 0.0 | 0.3 | |
| Total effect of Government decisions[1] | | -2.6 | 4.0 | 11.7 | 13.4 | 16.3 | 16.6 |
| *of which:* | | | | | | | |
| Departmental spending[1] | | -0.5 | 5.7 | 13.4 | 15.4 | 16.1 | 16.7 |
| Other spending measures[2] | | -2.2 | -1.6 | -1.5 | -1.5 | 1.0 | 1.0 |
| Indirect effects of Government decisions | | 0.0 | -0.1 | -0.2 | -0.5 | -0.8 | -1.0 |
| *Memo: March 2020 pre-measures forecast* | *44.3* | *51.8* | *55.7* | *57.6* | *59.8* | *60.6* | *62.5* |

[1] The change in 2024-25 is relative to a basline that assumes DEL would otherwise have remained constant as a share of GDP.
[2] Includes both scorecard and non-scorecard measures. See Annex A for more information.
Note: this table uses the convention that a negative figure means a reduction in PSNB. i.e. an increase in receipts or a reduction in spending will have a negative effect on PSNB.

## Public sector net borrowing

3.148 Public sector net borrowing fell from a high of £158.3 billion (10.2 per cent of GDP) in 2009-10 to 1.8 per cent by 2018-19. In our restated March 2019 forecast, we expected the deficit to shrink from £47.6 billion in 2019-20 to £33.3 billion in 2023-24. But, thanks to the fiscal loosening in the Budget, we now expect it to hit a six-year high of £66.7 billion in 2021-22 and to remain at £57.9 billion (2.2 per cent of GDP) in 2024-25.

Chart 3.7: Public sector net borrowing




Source: ONS, OBR

## Underlying forecast revisions

3.149 Borrowing in 2018-19 came in £2.5 billion lower than we anticipated in March 2019 (on a like-for-like basis). Nonetheless, on a pre-measures basis we have revised it up by £0.4 billion in 2019-20. This largely reflects upward revisions to borrowing-financed capital spending by local authorities and faster growth in the cost of R&D tax credits. We would not expect either to be reflected in the latest ONS outturns, which are currently still largely based on forecasts (ONS ones for local authorities and our March 2019 ones for tax credits).

3.150 Between 2020-21 and 2023-24, borrowing on a pre-measures basis has been revised up by an average of £3.1 billion a year (as Table 3.31 shows). This is more than explained by upward revisions to public sector net investment – both local authorities' capital spending and higher capital transfers associated with new student loans. That is partly offset by an underlying improvement in the current budget thanks to much lower debt interest spending.

## Government decisions

3.151 Government decisions raise borrowing in every year from 2020-21 onwards, nearly doubling the deficit in 2024-25. By 2024-25, £55.5 billion has been added to departmental spending, of which £14.6 billion has in effect been financed by using the direct fiscal savings from Brexit. The Government has also announced a net tax increase of £8.5 billion in that year, dominated by the effect of not going ahead with this April's cut in corporation tax. The indirect effects of the Budget measures offset roughly a quarter of their direct cost, more than explained by higher nominal GDP raising tax receipts and by the fact that a little over 10 per cent of the higher RDEL and Scottish Government current spending comes back to the Exchequer via higher pension contributions. The indirect fiscal cost of the new migration regime and the gain from the higher NLW are modest by comparison.

## Table 3.31: Changes to public sector net borrowing

| | £ billion | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Restated March 2019 forecast | 41.0 | 47.6 | 40.2 | 37.6 | 35.4 | 33.3 | |
| March 2020 forecast | 38.4 | 47.4 | 54.8 | 66.7 | 61.5 | 60.2 | 57.9 |
| Change | -2.5 | -0.2 | 14.6 | 29.1 | 26.0 | 26.9 | |
| Underlying revisions | -2.5 | 0.4 | 2.3 | 5.1 | 3.6 | 1.5 | |
| *of which:* | | | | | | | |
| Receipts[1] | -3.3 | -4.9 | 1.0 | 3.5 | 4.1 | 3.5 | |
| Debt interest | 0.5 | -2.0 | -6.7 | -6.6 | -7.7 | -8.5 | |
| Other spending[1] | 0.3 | 7.3 | 7.9 | 8.2 | 7.1 | 6.5 | |
| Total effect of Government decisions[2] | | -0.6 | 12.3 | 24.0 | 22.5 | 25.4 | 29.1 |
| *of which:* | | | | | | | |
| Current departmental spending[2] | | 2.9 | 15.2 | 27.0 | 31.2 | 34.9 | 38.9 |
| Capital departmental spending[2] | | -0.5 | 5.7 | 13.4 | 15.4 | 16.1 | 16.7 |
| Use of direct Brexit fiscal savings | | 0.0 | -4.3 | -5.0 | -7.1 | -11.3 | -14.6 |
| Receipts measures[3] | | -1.0 | -2.0 | -4.6 | -8.0 | -8.6 | -8.5 |
| Other spending measures[3] | | -2.1 | 1.1 | 0.3 | 0.7 | 2.6 | 3.9 |
| Indirect effects of Government decisions | | 0.0 | -3.3 | -7.1 | -9.7 | -8.4 | -7.2 |
| *of which:* | | | | | | | |
| Due to tax and spending measures | | 0.0 | -3.4 | -7.2 | -9.7 | -8.3 | -7.0 |
| Raising the National Living Wage | | 0.0 | 0.0 | -0.3 | -0.6 | -0.9 | -1.2 |
| New migration regime | | 0.0 | 0.0 | 0.3 | 0.5 | 0.8 | 1.0 |
| *Memo: March 2020 pre-measures forecast* | *38.4* | *48.1* | *42.5* | *42.7* | *39.0* | *34.9* | *28.8* |

[1] Excludes the impact of customs duties switch, which raises receipts and current spending by the same amount.
[2] The change in 2024-25 is relative to a baseline that assumes DEL would otherwise have remained constant as a share of GDP.
[3] Includes both scorecard and non-scorecard measures. See Annex A for more information.
Note: this table uses the convention that a negative figure means a reduction in PSNB. i.e. an increase in receipts or a reduction in spending will have a negative effect on PSNB.

### Cyclically adjusted net borrowing

3.152 On a pre-measures basis, our forecast for cyclically adjusted net borrowing is a little higher than our restated March 2019 forecast thanks to higher capital spending. As with the cyclically adjusted current budget, the direct effect of Budget tax and spending measures plus the migration and NLW policy changes raised cyclically adjusted net borrowing, while the indirect effects of the Budget measures are partly cyclical. As a result, Government decisions raise cyclically adjusted borrowing more than headline borrowing in the near term, but by similar amounts at the end of the forecast. On this measure, the deficit rises to 3.0 per cent of GDP in 2021-22 before falling back to 2.2 per cent by 2024-25.

## Box 3.6: The effect of the new migration regime on our fiscal forecast

In Box 2.4 we described the new 'points-based' immigration system that the Government intends to introduce from January 2021, aligning the rules for EU and non-EU migrants.[a] Relative to the current regime, this is more restrictive for EU migrants but modestly less so for non-EU migrants. Successful implementation of the new regime by January looks challenging.

In our economy forecast, we assume that this reduces the size of the population and total employment in 2024-25 by 0.4 per cent as it reduces net inward migration. This reduction is concentrated among people on lower-than-average earnings reflecting the £25,600 salary cap, so the effect on nominal GDP in 2024-25 is smaller at 0.3 per cent.

In this box we describe how these changes have affected our fiscal forecast. This is a narrower question than the full fiscal impact of migrants that some bodies have sought to answer, since our forecasts take departmental spending plans set by the Government – we do not forecast the cost of providing, say, health services or education to the population. This means that lower net inward migration raises departmental spending *per person*, rather than reducing the total.

As Table D shows, the largest effects on our forecast are the savings from lower welfare spending that is offset by the cost of lower income tax and NICs receipts. With departmental spending fixed, the additional costs from lower tax receipts on consumer spending and on company profits means the overall effect on our forecast is to add to borrowing. For all but welfare spending and income taxes, we have calculated these effects by assuming that the reduction in nominal tax bases is broadly in line with the reduction in nominal GDP. For those two items we have modelled the effects at a more granular level:

- For welfare benefits, we have drawn on DWP and HMRC administrative data that matches nationality at point of application for a National Insurance number, tax, earnings and benefit records. It suggests that fewer than 10 per cent of existing EEA benefit claimants would have a salary above the £25,600 threshold. Savings from lower migration under this salary threshold build up to £0.5 billion a year by 2024-25, equivalent to 0.4 per cent of working-age and child welfare spending in that year. (This means that the Budget announcement tightening migrants' access to benefits saves little as most of the benefit spending on this group ceases as a result of the migration regime.)
- For income tax and NICs, we estimate the effect of lower migration on wages and salaries based on the reduction in the size of the workforce and average earnings under the salary cap – this is a reduction of 0.3 per cent in 2024-25. We then calculate an effective tax rate on those lost earnings drawing on evidence from HMRC's Survey of Personal Incomes. This yields a loss of income tax and NICs receipts that rises to £0.6 billion in 2024-25, equivalent to 0.1 per cent of the total in that year.

These estimates are necessarily a simplification of what can be expected in reality and are subject to significant uncertainty. In particular, they focus only on those who would not qualify to come to the UK because they are below the income threshold. They do not take account of the potential deterrent effect of the new system on those above the income threshold (who would still incur extra costs and hassle to move to the UK), where losses would be larger. Nor do they take account of initially low-income migrants' earnings rising during their time in the UK.

## Table D: The effect of the new migration regime on our borrowing forecast

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Total effect on net borrowing | 0.0 | 0.0 | 0.3 | 0.5 | 0.8 | 1.0 |
| *of which:* | | | | | | |
| Welfare spending | 0.0 | 0.0 | 0.0 | -0.1 | -0.3 | -0.5 |
| Income tax and NICs receipts | 0.0 | 0.0 | 0.1 | 0.3 | 0.4 | 0.6 |
| VAT and excise duty receipts | 0.0 | 0.0 | 0.1 | 0.3 | 0.4 | 0.5 |
| Corporation tax receipts | 0.0 | 0.0 | 0.0 | 0.1 | 0.1 | 0.1 |
| Other receipts | 0.0 | 0.0 | 0.0 | 0.1 | 0.1 | 0.2 |

Alongside the Migration Advisory Committee's (MAC) latest report, Oxford Economics updated its analysis of EU migrants' fiscal contribution. This sought to answer the broader question than the one we answer in this box, including the cost of providing public services.[b] It estimated the net fiscal contribution of those who would be ineligible under a salary threshold of £30,000 – as the MAC had been asked to consider – to be *minus* £2,200 a year. The report also showed that the net fiscal contribution moved from negative to positive at a salary of around £20,000 (depending on age), so the net fiscal contribution of those below a £25,600 cap would be more negative than £2,200 a year. The difference between Oxford Economics' finding that cutting out such migration would boost the public finances and the negative effect the new migration regime change has had on our forecast reflects the fixed departmental spending totals. If departmental spending were 0.4 per cent lower in 2024-25, spending would be £2.0 billion lower, turning the negative impact on our forecast into a positive one.

[a] In most cases the existing rules for EU migrants also apply to those from the wider European Economic Area (EEA) and Switzerland. Irish citizens will continue to have freedom of movement within the Common Travel Area.
[b] Oxford Economics, *The Fiscal Impact of Immigration on the UK*, June 2018 and *The Fiscal Contribution of EU Migrants: Update and Scenario Analysis*, January 2020.

## Our latest forecast revisions in context

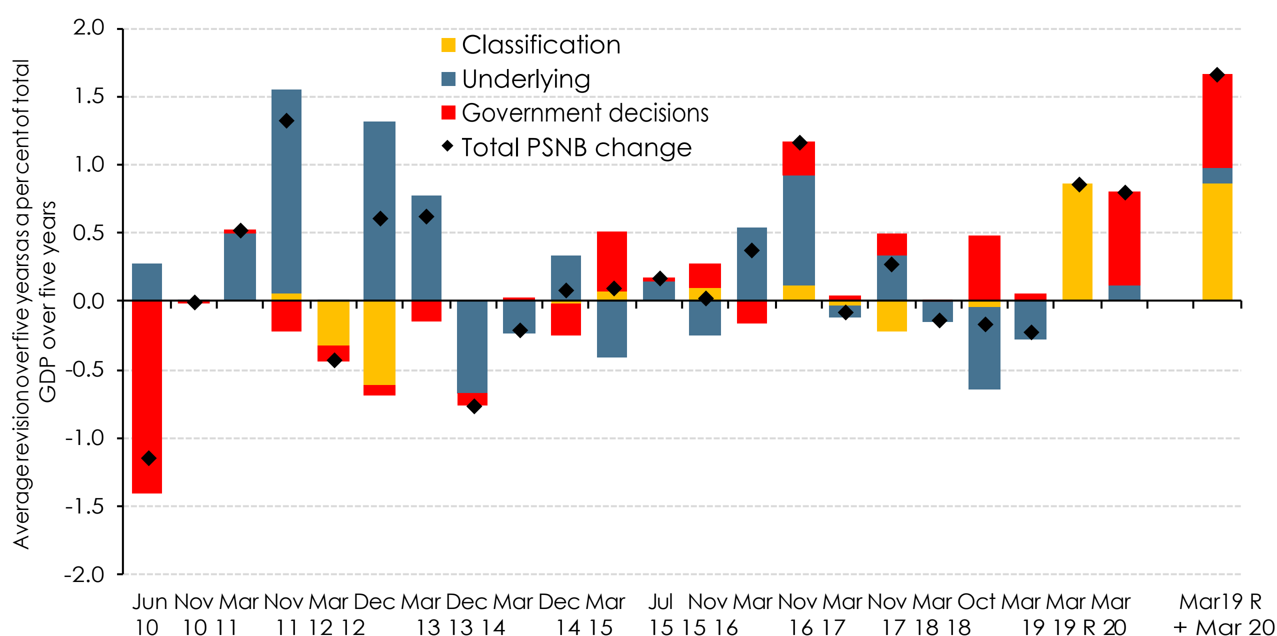
3.153 The forecasts for public sector net borrowing in this *EFO* are the twenty-first that we have published since the OBR was created in 2010 (together with one statistical restatement). As Chart 3.8 illustrates, the average upward revision to the deficit in this forecast of 0.8 per cent of GDP is the third largest over that period, exceeded only in November 2011 and November 2016.[20] These were both occasions on which we revised the outlook for potential GDP growth significantly lower, thanks largely to the EU referendum vote in the latter case.

3.154 Combining the classification changes that we presented in December when restating our March 2019 forecast – but that in normal circumstances would have been reflected alongside an updated pre-measures forecast and the effect of new policy decisions – the upward revision since our original March 2019 forecast is the largest we have made.

[20] Excluding the December 2019 restatement of the March 2019 forecast.

3.155 In contrast to previous large upward revisions – and despite the fact that almost a year has elapsed since our last full forecast – the underlying outlook for borrowing is little changed in this *EFO*. The average upward revision to the pre-measures deficit of just 0.1 per cent of GDP is the third smallest of the 13 upward revisions we have made over the past decade and the fourth smallest revision in either direction out of 21. By contrast, the Government's policy decisions have raised the deficit by 0.7 per cent of GDP on average, almost half as much again as the previous largest policy loosening in Budget 2018. The only time fiscal policy has been changed by a larger margin was the 1.4 per cent of GDP average fiscal tightening in the Coalition Government's first Budget in June 2010, when it set out its plans to reduce the post-crisis budget deficit that it had inherited.

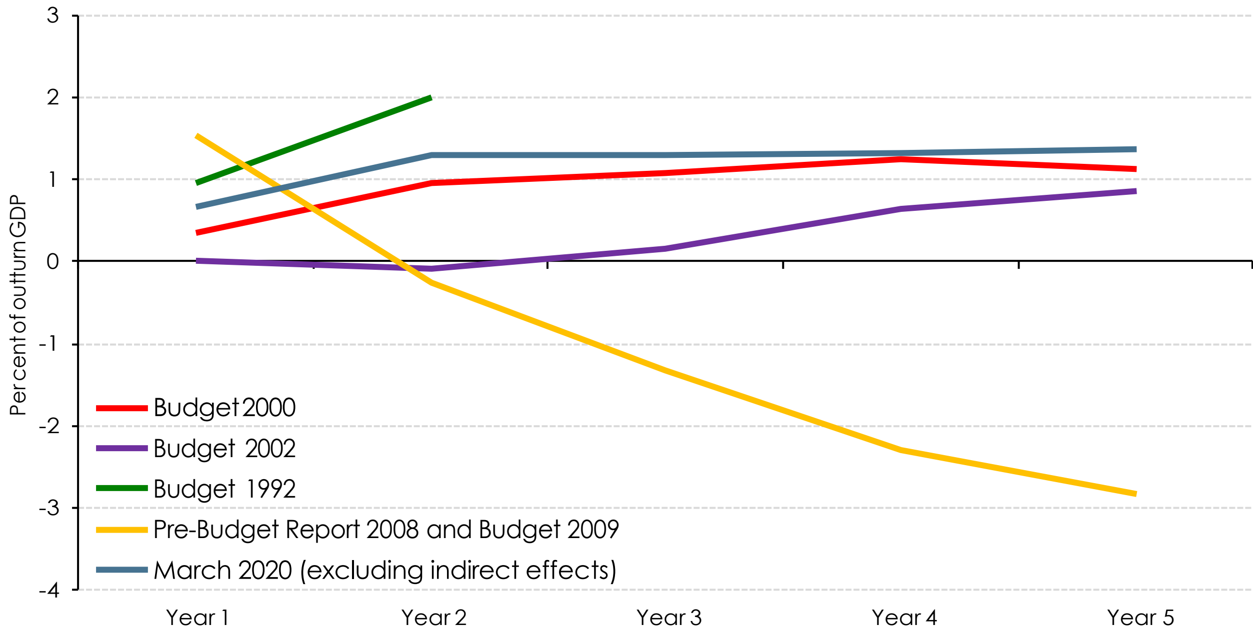
## Chart 3.8: Average revisions to borrowing since June 2010




Source: OBR

3.156 Looking further back in time (Chart 3.9), this looks like the largest planned sustained giveaway at any fiscal event since Norman Lamont's ill-fated pre-election Budget in 1992 (which was more than reversed within a matter of months after sterling crashed out of the European exchange rate mechanism). It is modestly greater than the giveaway in Gordon Brown's 2000 Budget, which – like this Budget – was dominated by public spending increases. Mr Brown judged that he had room for largesse then because of the robust performance of tax receipts, but this was soon dented by the bursting of the dotcom bubble.

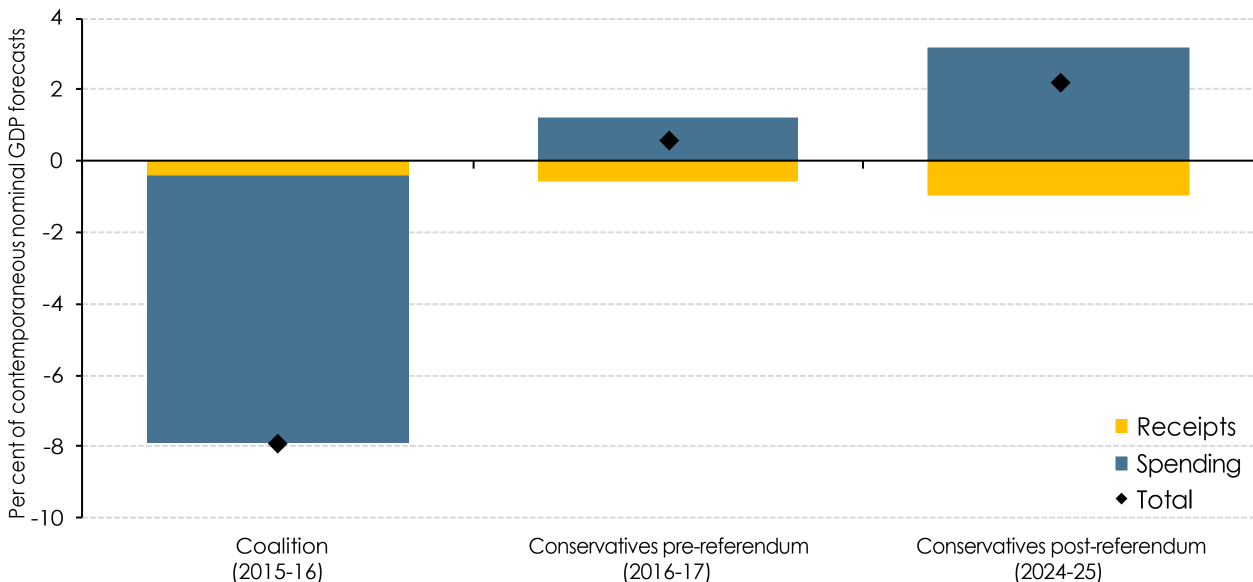
## Chart 3.9: Major fiscal giveaways and takeaways




Source: HM Treasury, OBR

3.157 The scale of the fiscal loosening in this Budget is all the more unusual for taking place at the first fiscal event following a general election, which governments in the past have tended to see as their best opportunity to take unpopular decisions on tax and spending. It is the latest in a series of giveaway fiscal events since the Conservatives won the 2015 election – and more particularly since the referendum vote to leave the EU in June 2016. As Chart 3.10 illustrates, fiscal events to date under the Conservatives have reversed almost a third of the fiscal tightening announced by the preceding Coalition Government, judging by their (roughly) estimated impact on borrowing at the current forecast horizon of 2024-25.

## Chart 3.10: Cumulative impact of policy decisions on borrowing in 2024-25




Note: March 2015 and July 2015 fiscal events have been combined in the Conservatives pre-referendum calculation because the Liberal Democrats put forward an alternative Budget ahead of the 2015 election.
Source: OBR

3.158 As we discuss in more detail in Chapter 4, the giveaways in this Budget move the Government further away from the 'fiscal objective' of a balanced budget that has been legislated for in its *Charter for Budget Responsibility* since January 2017, but which was already being downplayed ahead of the election. Having been on course to achieve a (tiny) budget surplus in 2023-24 in our October 2018 pre-measures forecast, our latest forecast points to a deficit of £60.2 billion (2.4 per cent of GDP in that year) – thanks in part to statistical classification changes but mostly to the giveaways in this and the 2018 Budget.

## Balance sheet aggregates

### Generating our balance sheet forecasts

3.159 We forecast several measures of the public sector balance sheet. For two decades, the headline measure has been public sector net debt (PSND). We forecast this in two stages:

- First, by forecasting the financial transactions that reconcile public sector net borrowing (PSNB) – the deficit on an accrued basis – with the public sector net cash requirement (PSNCR) – the deficit on a cash basis. These include loans and repayments between the public and private sectors, sales or purchases of financial assets, Bank of England schemes, and various timing effects.

- Second, we forecast the valuation effects and (when necessary) impact of classification changes that reconcile the PSNCR with the year-on-year change in PSND.

3.160 Table 3.32 sets out our latest forecast for these lines. Table 3.33 shows changes relative to our restated March 2019 forecast, which reflected several ONS statistical changes.

3.161 We use similar approaches to forecast other balance sheet aggregates, starting from the relevant deficit measure and adding other elements as required.

## Table 3.32: Sources of year-on-year changes in public sector net debt

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Year-on-year change in PSND (a+b+c+d) | 25.4 | 19.4 | 8.9 | 72.5 | 69.2 | 62.2 |
| Public sector net borrowing (a) | 47.4 | 54.8 | 66.7 | 61.5 | 60.2 | 57.9 |
| Financial transactions (b) | -15.1 | -29.5 | -60.3 | 10.8 | 6.3 | 12.8 |
| *of which:* | | | | | | |
| DEL net lending | 5.5 | 6.0 | 4.3 | 4.5 | 2.0 | 2.0 |
| Help to Buy outlays | 3.6 | 3.8 | 2.2 | 2.5 | | |
| Other housing schemes | 0.4 | 0.3 | | | | |
| Devolved administrations | 0.3 | 0.5 | | | | |
| Other DEL | 1.3 | 1.7 | | | | |
| DEL beyond current Spending Review | | | 2.7 | 2.7 | 2.6 | 2.6 |
| Allowance for shortfall | -0.1 | -0.3 | -0.6 | -0.6 | -0.6 | -0.6 |
| Other government net lending | 6.1 | 6.8 | 7.3 | 7.0 | 5.5 | 4.9 |
| Student loan outlays[1] | 9.3 | 9.6 | 10.0 | 10.5 | 11.0 | 11.6 |
| Student loan repayments[2] | -3.3 | -3.7 | -4.2 | -4.6 | -5.0 | -5.4 |
| Loan to Ireland | -1.6 | -1.6 | | | | |
| Scottish Government | 0.7 | 0.8 | 0.8 | 0.9 | 0.9 | 0.9 |
| UK Export Finance | 0.6 | 1.9 | 1.4 | 1.2 | 0.5 | 0.2 |
| Other AME | 1.3 | 1.3 | 1.1 | 1.4 | 0.8 | 0.4 |
| Help to Buy repayments | -0.9 | -1.5 | -2.0 | -2.4 | -2.7 | -2.8 |
| Sales or purchases of financial assets | -5.4 | -10.5 | -3.5 | -4.1 | -3.6 | -3.3 |
| Student loans | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| RBS shares | 0.0 | -3.8 | -3.6 | -4.2 | -3.3 | -3.3 |
| UKAR asset sales and rundown | -4.7 | -5.5 | 0.0 | 0.0 | -0.3 | 0.0 |
| Other sales | -0.7 | -1.2 | 0.0 | 0.0 | 0.0 | 0.0 |
| Bank of England schemes | -14.3 | -43.7 | -63.4 | 0.0 | 0.0 | 0.0 |
| Cash flow timing effects | -7.0 | 11.9 | -4.9 | 3.4 | 2.4 | 9.2 |
| Student loan interest[2] | 2.8 | 2.9 | 3.2 | 3.8 | 4.5 | 4.9 |
| Corporation tax | -6.8 | -0.8 | 2.4 | 1.9 | 1.6 | 1.6 |
| Other receipts | 5.7 | 7.0 | 5.2 | 4.0 | 4.6 | 4.3 |
| Funded public pension schemes | -1.7 | -1.9 | -1.9 | -2.0 | -2.1 | -2.1 |
| Index-linked gilt uplift[3] | -10.4 | 0.5 | -13.9 | -7.0 | -9.4 | -2.9 |
| Other gilt accruals | 4.4 | 4.6 | 4.4 | 5.0 | 5.4 | 5.6 |
| Other expenditure | -1.0 | -0.5 | -4.4 | -2.3 | -2.2 | -2.2 |
| *Public sector net cash requirement (a+b)* | *32.3* | *25.3* | *6.3* | *72.2* | *66.5* | *70.8* |
| Valuation effects (c) | -6.9 | -5.9 | 2.6 | 0.2 | 2.7 | -8.6 |
| *of which:* | | | | | | |
| Gilt premia | -13.1 | -8.5 | -8.0 | -7.5 | -7.1 | -8.6 |
| Asset Purchase Facility gilt premia | 3.2 | 1.5 | -3.2 | 0.8 | 0.5 | -2.9 |
| Index-linked gilts uplift[3] | 10.4 | -0.5 | 13.9 | 7.0 | 9.4 | 2.9 |
| International reserves | -7.4 | 1.6 | -0.1 | -0.1 | 0.0 | 0.0 |
| ONS statistical changes (d) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |

[1] This records the non-spending part of outlays, the remainder is recorded as capital transfers.

[2] Cash payments of interest on student loans are included within 'Student loan repayments', as we cannot easily separate them from repayments of principal. To prevent double counting, the 'student loan interest' timing effect removes all accrued interest.

[3] This reconciliation to the public sector net cash requirement does not affect public sector net debt.

## Table 3.33: Changes to the public sector net debt profile since March 2019

| | £ billion | | | | |
|---|---|---|---|---|---|
| | Forecast | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
| Year-on-year change in PSND (a+b+c+d) | -12.5 | 26.6 | 37.8 | 26.9 | 25.9 |
| Public sector net borrowing (a) | -0.2 | 14.6 | 29.1 | 26.0 | 26.9 |
| Financial transactions (b) | -0.1 | 11.9 | 8.0 | 2.5 | 1.5 |
| *of which:* | | | | | |
| DEL net lending | -0.5 | -0.4 | -1.6 | -1.9 | -0.3 |
| Help to Buy outlays | -0.4 | -0.4 | -1.0 | -1.2 | |
| Other housing schemes | -0.1 | -0.3 | | | |
| Devolved administrations | -0.2 | 0.0 | | | |
| Other DEL | 0.0 | 0.3 | | | |
| DEL beyond current Spending Review | - | - | -0.6 | -0.7 | -0.3 |
| Allowance for shortfall | 0.2 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other government net lending | -1.3 | -1.2 | -1.9 | -1.3 | -2.0 |
| Student loan outlays[1] | -0.6 | -0.9 | -1.2 | -1.2 | -1.2 |
| Student loan repayments[2] | -1.0 | -1.4 | -1.7 | -2.0 | -2.1 |
| Loan to Ireland | 0.0 | 0.0 | | | |
| Scottish Government | 0.2 | 0.1 | 0.4 | 0.4 | 0.8 |
| UK Export Finance | 0.0 | 0.9 | 0.6 | 1.1 | 0.4 |
| Other AME | -0.1 | 0.2 | 0.1 | 0.5 | 0.2 |
| Help to Buy repayments | 0.2 | 0.0 | -0.1 | 0.0 | 0.1 |
| Sales or purchases of financial assets | 13.0 | -3.3 | 5.2 | 5.7 | 2.4 |
| Student loans | 4.6 | 4.7 | 5.0 | 5.2 | 0.0 |
| RBS shares | 3.6 | -1.4 | 0.1 | 0.5 | 2.6 |
| UKAR asset sales and rundown | 4.9 | -5.5 | 0.0 | 0.0 | -0.3 |
| Other sales | -0.1 | -1.2 | 0.0 | 0.0 | 0.0 |
| Bank of England schemes | -14.3 | 7.5 | 6.9 | 0.0 | 0.0 |
| Cash flow timing effects | 3.1 | 9.3 | -0.6 | 0.1 | 1.3 |
| Student loan interest[2] | 0.0 | -0.1 | -0.1 | -0.1 | 0.1 |
| Corporation tax | -2.2 | 1.9 | 0.6 | 0.2 | 0.0 |
| Other receipts | 1.2 | 1.3 | 0.5 | -0.4 | -0.1 |
| Funded public pension schemes | 0.1 | 0.1 | 0.1 | 0.1 | 0.1 |
| Index-linked gilt uplift[3] | 2.2 | 3.1 | 0.4 | 0.4 | 0.9 |
| Other gilt accruals | 0.3 | 0.5 | 0.5 | 0.6 | 0.7 |
| Other expenditure | 1.6 | 2.5 | -2.5 | -0.7 | -0.4 |
| *Public sector net cash requirement (a+b)* | *-0.3* | *26.4* | *37.1* | *28.5* | *28.4* |
| Valuation effects (c) | -12.1 | 0.2 | 0.7 | -1.7 | -2.4 |
| *of which:* | | | | | |
| Gilt premia | -5.0 | 0.9 | -0.8 | -1.2 | -1.6 |
| Asset Purchase Facility gilt premia | 2.9 | 1.0 | 2.2 | 0.2 | 0.2 |
| Index-linked gilts uplift[3] | -2.2 | -3.1 | -0.4 | -0.4 | -0.9 |
| International reserves | -7.9 | 1.4 | -0.2 | -0.2 | -0.2 |
| ONS statistical changes (d) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |

[1] This records the non-spending part of outlays, the remainder is recorded as capital transfers.

[2] Cash payments of interest on student loans are included within 'Student loan repayments', as we cannot easily separate them from repayments of principal. To prevent double counting, the 'student loan interest' timing effect removes all accrued interest.

[3] This reconciliation to the public sector net cash requirement does not affect public sector net debt.

## Public sector net cash requirement

3.162 Table 3.32 shows that the PSNCR is positive in every year of the forecast, with financing for the deficit being the main driver. Financial transactions reduce the PSNCR up to 2021-22, dominated by repayment of the Bank of England's Term Funding Scheme (TFS) loans. In the final three years of the forecast, financial transactions add to the PSNCR as government lending outweighs proceeds from asset sales.

3.163 Table 3.33 shows changes since our restated March 2019 forecast. PSNCR is higher in all years from 2020-21, thanks to higher borrowing (largely as a result of Budget measures) and TFS loans being repaid earlier than we had previously assumed (which brings cash receipts forward into 2019-20). The cancellation and delay of asset sales increases PSNCR in all years except 2020-21, which benefits from sales that have slipped from 2019-20.

### Loans and repayments

3.164 As regards loans and repayments between the public and private sectors:

- The Government's forecasts for lending within the DEL envelope have been revised down in the years to 2022-23, largely reflecting lower expected lending through the Help to Buy: Equity Loan scheme. Help to Buy lending has been reduced both by a policy announced at this Budget that restricts eligibility and a change to the forecasting methodology that brings it more into line with our central forecast.

- We have revised down financial transactions relating to student loan outlays – i.e. the portion of outlays that is not treated as spending. Despite revising up outlays in total this is outweighed by a greater proportion being recorded as spending rather than lending. Policy changes have modestly reduced outlays.

- In the Budget, the Government has announced plans to increase lending through UK Export Finance. UKEF's total lending capacity has been increased by £3 billion, adding to the £2 billion increase announced at Budget 2018.

### Sales and purchases of financial assets

3.165 At Budget 2019 the Government planned to sell £42 billion of financial assets between 2019-20 and 2023-24. Chart 3.11 shows that this has been revised down by £11 billion in this forecast, thanks to various delays and cancellations. The largest effect is in 2019-20, where proceeds have been revised down from £16.4 billion to £5.4 billion. Overall:

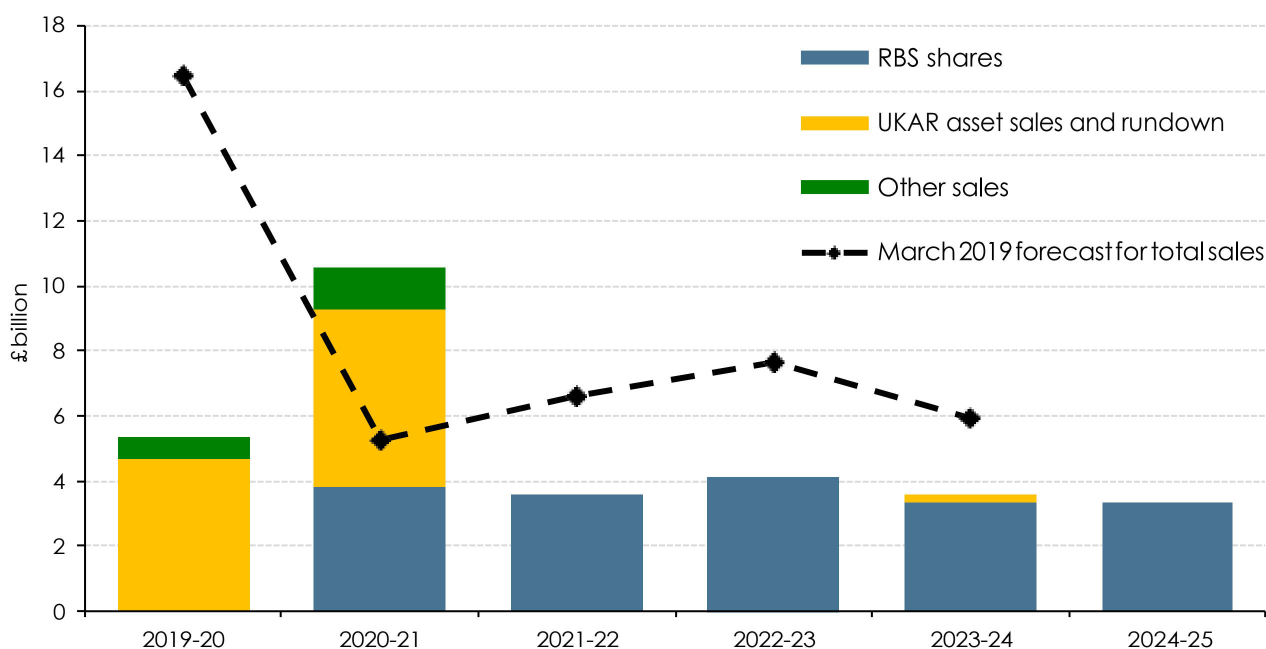
- Sales of Plan 1 student loans have been cancelled. The Treasury's review of the sales concluded that "*Following the Office for National Statistics' change in the accounting treatment of student loans, loan sales now have a significant negative impact on public sector net borrowing*" and that "*The government has therefore taken the decision that it will no longer proceed with further sales of student loans.*"[21] The real-world impact of

[21] HM Treasury, *Review of the student loan programme: Budget 2020*, March 2020.

student loan sales is unaffected by the way the ONS accounts for them, so this change of heart might suggest to the cynical that the previous policy – of selling loans for less than they are valued on the government's books, justified with reference to the 'value for money' criteria in the Treasury's Green Book – was undertaken at least in part to exploit the 'fiscal illusions' created by the previous accounting treatment and thereby create the impression that by selling loans the government was strengthening the public finances. (We discussed this perverse incentive in Box 4.4 of our October 2018 *EFO*.) The cancellation of the Plan 1 sales foregoes cash proceeds of £11.3 billion. This raises PSND, but also removes the associated capital transfers recorded in spending by £8.5 billion, which would otherwise have raised public sector net financial liabilities (better reflecting their effect on fiscal sustainability more broadly).

- The final large sale of UKAR assets has been delayed and is now expected to be completed in early 2020-21 rather than late 2019-20.
- The Government has not sold any RBS shares so far in 2019-20 and we judge that it is unlikely that any sale will occur in the remainder of the year. The Government still plans to sell all its RBS shares, but now over a longer period up to 2024-25. Our forecast for overall proceeds has been reduced in line with the lower RBS share price.
- Sales of further tranches of spectrum licenses have been delayed. We have revised up expected gross proceeds from £0.5 billion in 2019-20 to £1.3 billion in 2020-21, which reflects Ofcom dropping some coverage obligations and the Government agreeing to pay half the construction costs, in return for the four main mobile operators delivering a 'Shared Rural Network'.

## Chart 3.11: Proceeds from financial asset sales




Source: HM Treasury, OBR

### Bank of England schemes

3.166 As of 19 February, £13.8 billion of TFS loans had been repaid in 2019-20 rather than at maturity as we had previously assumed. We have assumed this will rise to £14.3 billion by the end of the year and that these repayments relate to loans due in 2020-21. We have also assumed that some loans due in 2021-22 will be repaid early in 2020-21.

### Timing effects

3.167 As regards cashflow timing effects and abstracting from the RPI uplift on index-linked gilts (which offsets in valuation effects):

- The cancellation of the corporation tax cut discussed earlier in this chapter increases cash receipts by £2.1 billion relative to accruals.

- Cash VAT receipts are forecast to be increased by £3.6 billion relative to accrued receipts this year from a delay in the payment date for VAT on imports from outside the EU. This has a large effect in 2019-20, when there will in effect be only 11 months of import VAT payments, with much smaller continuing effects in subsequent years.

## Public sector net debt

3.168 Higher nominal GDP reduces PSND relative to GDP in all years of the forecast, on average by 1.1 percentage points. Underlying forecast revisions also reduce cash debt in all years, though by decreasing amounts across the forecast. Government policy decisions add progressively more to debt, reaching £125 billion in 2024-25. Consequently, net debt is now essentially flat as a share of GDP in the later years of the forecast (once the Bank of England's TFS loans have been repaid), having been declining in our March 2019 forecast.

3.169 As regards underlying forecast revisions, cumulative borrowing raises cash debt modestly by 2023-24, while a weaker pound raises the sterling value of the foreign currency reserves by a broadly offsetting amount. The early repayment of TFS loans reduces debt in the early years of the forecast, but that effect unwinds by 2021-22 once they have all been repaid.

3.170 As regards Government decisions:

- The direct effects of the Budget package on public sector net borrowing adds progressively more to debt over the period, reaching £148 billion in 2024-25.

- Delays and cancellations to asset sales also add steadily to debt. Delaying the sale of UKAR and RBS assets increases debt at the start of the period, but this largely unwinds over the forecast. The cancellation of student loans sales raises our debt forecast by increasing amounts due to the proceeds foregone. This accounts for the majority of the £11 billion upward revision to debt from this source in 2024-25.

- The wider effects of policy measures on the economy – including the temporary effects of the Budget package and the persistent ones of the new migration regime and

higher path for the National Living Wage – partly offset these direct effects. Overall they reduce debt by £36 billion in 2024-25.

## Table 3.34: Changes to public sector net debt since March 2019

| | Per cent of GDP | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Restated March 2019 forecast | 82.2 | 81.3 | 78.2 | 74.3 | 73.6 | 72.7 | |
| March 2020 forecast | 80.6 | 79.5 | 77.4 | 75.0 | 75.4 | 75.6 | 75.2 |
| Like-for-like change | -1.5 | -1.8 | -0.8 | 0.7 | 1.9 | 2.9 | |
| *of which:* | | | | | | | |
| Change in nominal GDP[1] | -1.3 | -1.0 | -1.1 | -1.2 | -1.0 | -0.9 | |
| Change in cash level of net debt | -0.3 | -0.8 | 0.4 | 1.9 | 2.9 | 3.8 | |
| | £ billion | | | | | | |
| Restated March 2019 forecast | 1,779 | 1,817 | 1,810 | 1,781 | 1,827 | 1,870 | |
| March 2020 forecast | 1,774 | 1,799 | 1,818 | 1,827 | 1,900 | 1,969 | 2,031 |
| Like-for-like change in cash debt | -6 | -18 | 8 | 46 | 73 | 99 | |
| *of which:* | | | | | | | |
| Underlying forecast revisions | -6 | -29 | -20 | -7 | -5 | -3 | |
| Public sector net borrowing (pre-measures) | -3 | -2 | 0 | 5 | 9 | 10 | |
| Financial transactions (pre-measures) | -4 | -17 | -7 | 0 | 0 | 1 | |
| Valuation changes | 1 | -10 | -13 | -12 | -14 | -15 | |
| Effect of Government decisions | | 11 | 28 | 54 | 78 | 102 | 125 |
| Affecting public sector net borrowing | | -1 | 15 | 46 | 78 | 112 | 148 |
| Affecting financial transactions | | 13 | 11 | 12 | 16 | 17 | 12 |
| Indirect effects | | -1 | 3 | -5 | -16 | -27 | -36 |

[1] Non-seasonally adjusted GDP centred end-March.

## Central government net cash requirement

3.171 The central government net cash requirement (CGNCR) is a key determinant of the Government's net financing requirement. Table 3.35 reconciles CGNCR with PSNCR (by removing transactions associated with local authorities and public corporations) and Table 3.36 sets out the changes in this reconciliation since March. Relative to the restated March forecast, public corporations' net cash requirement has changed largely due to the profile of Bank of England TFS loan repayments, while CGNCR ex is £20.6 billion higher on average across the forecast largely reflecting the Government's policy changes.

3.172 The inclusion of Bradford & Bingley (B&B), Northern Rock Asset Management (NRAM) and Network Rail in the central government sector means that the CGNCR is not simply a measure of the cash required by the Exchequer to fund its operations. Excluding these bodies to forecast the Government's net financing requirement involves adjustments for:[22]

[22] The Government is confirming the financing remit for 2019-20 and setting the remit for 2020-21 alongside this Budget. The OBR provides the Government with the forecast of the CGNCR for this purpose, but plays no further role in the derivation of the net financing requirement.

- The difference between the net cash received by B&B and NRAM and that transferred to central government. This adjustment ceases from 2020-21 onwards as our forecast assumes that the rundown of bodies will have been completed next year.

- The Treasury financing Network Rail's new and maturing debt for a fee. Refinancing needs are estimated at £2.6 billion over the forecast.

## Table 3.35: Reconciliation of PSNCR and CGNCR

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Public sector net cash requirement (NCR) | 32.3 | 25.3 | 6.3 | 72.2 | 66.5 | 70.8 |
| *of which:* | | | | | | |
| Local authorities and public corporations NCR | -6.2 | -34.7 | -62.0 | 6.6 | 7.2 | 3.1 |
| Central government (CG) NCR own account | 38.5 | 60.0 | 68.3 | 65.6 | 59.3 | 67.7 |
| CGNCR own account | 38.5 | 60.0 | 68.3 | 65.6 | 59.3 | 67.7 |
| Net lending within the public sector | 5.7 | 4.9 | 4.8 | 4.8 | 4.7 | 4.6 |
| CG net cash requirement | 44.2 | 64.8 | 73.1 | 70.4 | 64.0 | 72.2 |
| B&B and NRAM adjustment | -0.5 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Network Rail adjustment | -0.6 | 0.4 | -0.1 | -0.5 | 0.0 | 0.3 |
| CGNCR ex. B&B, NRAM and Network Rail | 43.1 | 65.3 | 73.0 | 69.9 | 64.0 | 72.6 |

## Table 3.36: Changes in the reconciliation of PSNCR and CGNCR

| | £ billion | | | | |
|---|---|---|---|---|---|
| | Forecast | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 |
| Public sector net cash requirement (NCR) | -0.3 | 26.4 | 37.1 | 28.5 | 28.4 |
| *of which:* | | | | | |
| Local authorities and public corporations NCR | -14.0 | 13.0 | 9.9 | 3.7 | 4.4 |
| Central government (CG) NCR own account | 13.7 | 13.4 | 27.2 | 24.8 | 23.9 |
| CGNCR own account | 13.7 | 13.4 | 27.2 | 24.8 | 23.9 |
| Net lending within the public sector | 1.5 | 0.4 | 0.1 | -0.2 | -0.6 |
| CG net cash requirement | 15.1 | 13.8 | 27.3 | 24.6 | 23.4 |
| B&B and NRAM adjustment | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Network Rail adjustment | 0.0 | 0.0 | 0.2 | 0.0 | -0.8 |
| CGNCR ex. B&B, NRAM and Network Rail | 15.1 | 13.8 | 27.5 | 24.6 | 22.6 |

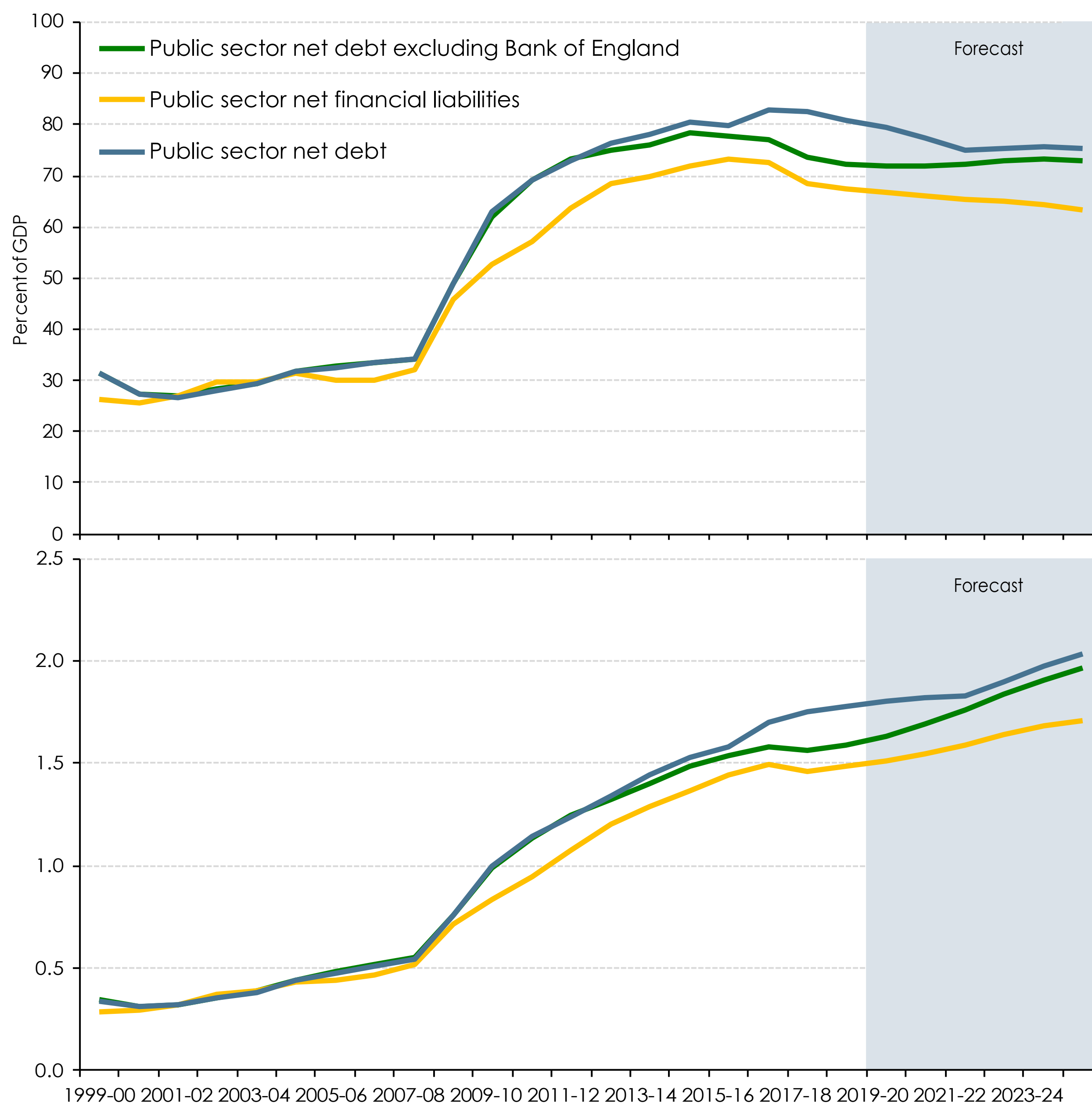
### Alternative balance sheet aggregates

3.173 Our *Fiscal risks reports* have discussed various ways in which PSND is not a reliable metric for assessing the underlying health of the public finances. It includes only a limited range of liabilities and an even smaller range of assets. This makes it susceptible to 'fiscal illusions' – when movements in a fiscal aggregate do not reflect true changes in the underlying health of the public finances – particularly when selling illiquid assets.

3.174 Alternative metrics often do a better job than PSND of reflecting the underlying picture, although none is perfect. PSND excluding the Bank of England removes the distortions caused by the TFS, while public sector net financial liabilities (PSNFL) provides a more

realistic picture of the effect of asset sales. Chart 3.12 shows that the paths of both measures are much smoother than PSND, especially when the TFS loans are being repaid.

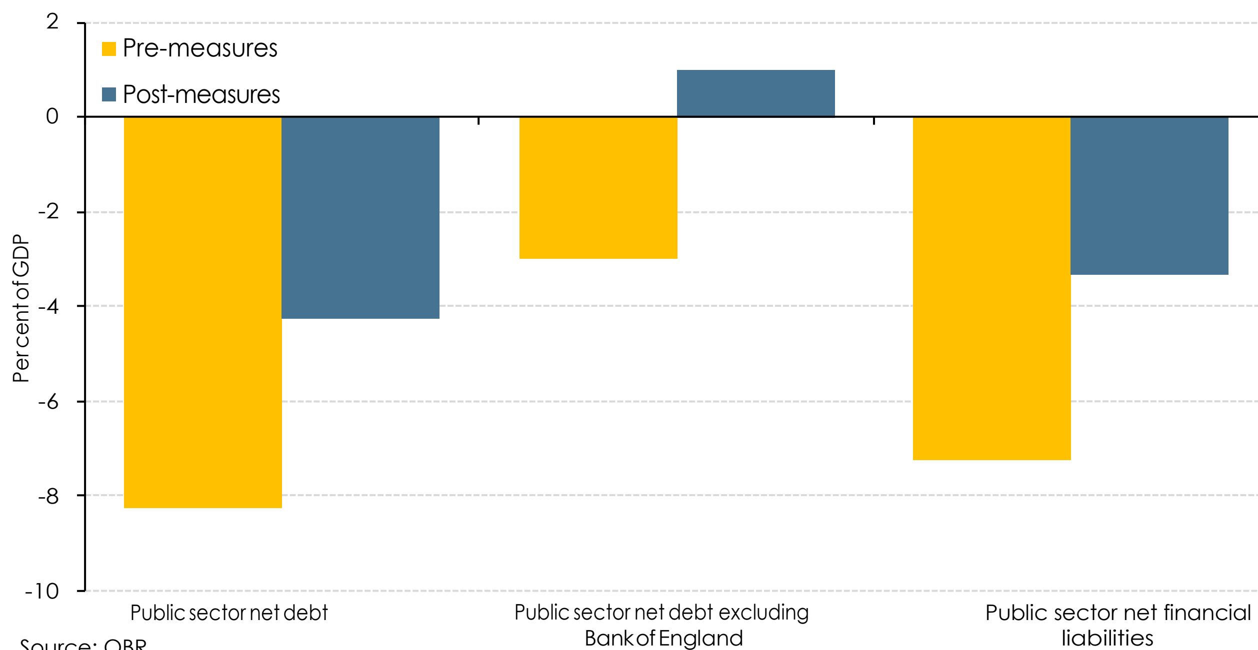
## Chart 3.12: The public sector balance sheet: various measures




Source: ONS, OBR

3.175 Chart 3.13 shows the change between 2019-20 and 2024-25 for each of these metrics on a pre- and post-measures basis. All three fall pre-measures, with the measure excluding the Bank of England falling the least. The post-measures improvements are around 4 per cent of GDP smaller, with PSND excluding the Bank of England actually rising slightly. Headline PSND still falls as TFS loans are repaid and PSNFL still declines as assets not included in PSND (such as student loans and those of funded pensions schemes) increase in value.

## Chart 3.13: Balance sheet changes between 2019-20 and 2024-25




Source: OBR

## Financing and the balance sheet

3.176 Our debt interest forecast requires us to judge how changes in PSND translate into movements in the stocks of assets and liabilities on the public sector balance sheet.

3.177 At each Budget and Spring Statement, the Government states how it intends to meet its financing needs in the 'financing remit'.[23] This calculates the gross financing requirement from our forecast for CGNCR ex, the amount of gilts redeeming, any plans for additional financing of the foreign exchange reserves and adjustments as necessary for any under- or over-financing from the previous year. Alongside this Budget the Government has confirmed the financing arithmetic for 2019-20 and published initial plans for 2020-21.

3.178 The Government usually meets most of its gross financing requirement by issuing gilts.[24] The rest is met via changes to the stock of Treasury bills, from NS&I products (such as premium bonds) or from other sources. As Table 3.37 shows, 89 per cent of the 2019-20 gross financing requirement (which is largely complete) is expected to be met by issuing gilts.

3.179 In our March 2019 forecast, the remit for 2019-20 intended index-linked gilts (ILGs) to make up 20.7 per cent of all gilts issued. Since then the Government has revised the remit several times, expanding gilt sales by £22.7 billion in anticipation of larger financing needs. The extra sales have mostly been of conventional gilts, so the proportion of ILGs in 2019-20 issuance is now expected to be just 16.5 per cent.

[23] HM Treasury, *Debt management report 2019-20*, 2020.
[24] The financing remit does not allocate all gilt issuance (leaving the DMO with some flexibility through the year), so we assume that the unallocated portion will ultimately be allocated in proportion to announced sales. We also assume that changes in the DMO's net cash position are met entirely by reductions in its assets.

3.180 In our March 2019 forecast, and in line with the Government's stated plan, the proportion of ILGs was assumed to fall by 1.5 percentage points each year over the remainder of the forecast. Had our forecast at the time extended to 2024-25, the ILG proportion would have fallen to 13.2 per cent in that year. In its remit for 2020-21, the Government plans to issue 13.2 per cent of gilts as ILGs. So absent any further clarification of what this means for future financing plans, we have assumed that the proportion of ILGs will remain at this level.

3.181 In the remit for 2020-21, Government has accommodated the decline in the proportion of ILGs issued primarily by issuing 'short' (up to 7 years) conventional gilts. Our March 2019 forecast assumed these would make up 27.9 per cent of total gilt issuance whereas the plan is now 33.7 per cent. The higher share of shorter maturity gilts reduces debt interest costs (all else equal), but at the expense of a greater sensitivity to gilt rate movements as the debt will have to be rolled over sooner.

## Table 3.37: Total gross financing

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Central government net cash requirement[1] | 43.1 | 65.3 | 73.1 | 69.9 | 64.0 | 72.6 |
| Gilt redemptions | 98.9 | 97.6 | 79.3 | 73.3 | 71.8 | 90.6 |
| Financing for the reserves | 6.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Change in DMO cash position[2] | 0.5 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Total gross financing | 148.5 | 162.9 | 152.4 | 143.2 | 135.8 | 163.2 |
| *of which:* | | | | | | |
| Conventional gilts | 110.2 | 133.6 | 126.8 | 119.0 | 112.7 | 136.1 |
| Index-linked gilts | 22.1 | 22.7 | 21.5 | 20.2 | 19.1 | 23.1 |
| Treasury bills | 6.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| NS&I | 10.1 | 6.0 | 4.0 | 4.0 | 4.0 | 4.0 |
| Other central government | 0.1 | 0.6 | 0.1 | 0.0 | 0.0 | -0.1 |

[1] Excluding Northern Rock, Bradford and Bingley, and Network Rail.
[2] Change in Debt Management Office cash position.

3.182 Table 3.38 shows how we expect the public sector's debt liabilities and liquid financial assets to evolve over the forecast.[25] The table is presented in line with that used by the ONS in the monthly public sector finances release: general government and non-financial public corporations are presented gross, but the Bank of England is shown only on a net basis.

3.183 The overall level of public sector debt liabilities reduces slightly over the forecast with the stock of index-linked gilts declining most as a result of the Government's plan to reduce its exposure to these instruments. The stock of conventional gilts rises across the forecast as they remain the Government's main source of financing. Assets decline as a share of GDP, most notably in the reserves; in recent years the cash level of the reserves has been boosted by regular financing through the remit and by a recent temporary boost to the reserves. The Government does not plan more cash injections in the forecast period and so the level declines as a share of GDP. By far the largest contribution to falling debt comes from the Bank of England as reserves fall when TFS loans are repaid.

[25] A similar table for PSNFL assets and liabilities is presented in the supplementary fiscal tables accompanying this forecast.

## Table 3.38: The composition of public sector net debt

| | Per cent of GDP[1] | | | | | |
|---|---|---|---|---|---|---|
| | Forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Public sector debt liabilities[2] (a) | 81.3 | 80.8 | 81.2 | 81.3 | 81.3 | 81.0 |
| *of which:* | | | | | | |
| Conventional gilts | 46.9 | 47.1 | 47.3 | 48.2 | 48.8 | 49.1 |
| Index-linked gilts | 19.7 | 19.2 | 19.6 | 19.2 | 18.8 | 18.4 |
| T-bills | 3.6 | 3.4 | 3.3 | 3.2 | 3.1 | 3.0 |
| NS&I | 7.8 | 7.8 | 7.7 | 7.6 | 7.5 | 7.4 |
| Other central government | 2.9 | 2.8 | 2.7 | 2.6 | 2.5 | 2.4 |
| Local government[3] | 0.9 | 1.0 | 1.1 | 1.2 | 1.2 | 1.3 |
| Non-financial public corporations[4] (b) | -0.6 | -0.6 | -0.6 | -0.6 | -0.6 | -0.6 |
| Public sector liquid assets[2] (c) | 9.4 | 8.8 | 8.8 | 8.5 | 8.2 | 8.1 |
| *of which:* | | | | | | |
| Reserves | 5.6 | 5.3 | 5.1 | 5.0 | 4.8 | 4.6 |
| Other central government | 1.9 | 1.8 | 1.7 | 1.7 | 1.6 | 1.5 |
| Local government[3] | 1.0 | 0.8 | 0.8 | 0.7 | 0.7 | 0.7 |
| Non-financial public corporations[4] | 0.9 | 0.9 | 1.2 | 1.1 | 1.1 | 1.3 |
| Bank of England net contribution (d) | 7.6 | 5.5 | 2.7 | 2.5 | 2.5 | 2.3 |
| Public sector net debt (PSND) (a-c+d) | 79.5 | 77.4 | 75.0 | 75.4 | 75.6 | 75.2 |
| *Memo: PSND excluding Bank of England (a-c)* | *71.9* | *71.9* | *72.3* | *72.9* | *73.1* | *72.9* |
| *Memo: general government gross debt (a-b)* | *81.9* | *81.4* | *81.8* | *82.0* | *81.9* | *81.6* |

[1] Non-seasonally adjusted GDP centred end-March.
[2] Excluding the Bank of England.
[3] Net of debt liabilities / liquid assets held by central government.
[4] Net of debt liabilities / liquid assets held by central and local government.
[5] Largely reserves issued to fund TFS loans and the APF's corporate bond purchases, plus premia on the APF's conventional gilt holdings.

## Financial sector interventions

3.184 Table 3.39 updates our estimate of the net direct effect on the public finances of the Government's interventions in the financial sector during the financial crisis and subsequent recession. This is not an attempt to quantify their overall effect on the public finances relative to a counterfactual where the Government had not intervened as the crisis unfolded. The costs of the crisis would almost certainly have been much greater in the absence of direct interventions to restore the financial system to stability.[26]

3.185 In total, £136.6 billion was disbursed by the Treasury during and following the crisis. By mid-February 2020, principal repayments had amounted to £97.3 billion, up slightly relative to March 2019, reflecting ongoing repayments from UKAR. This has fed through to a smaller net cash shortfall of £12.5 billion.

3.186 As of mid-February, virtually all the Treasury's loans to the financial sector had been repaid. The value of its RBS shares had fallen to £16.7 billion,[27] down from the £18.2 billion

[26] We discussed the fiscal implications of financial crises in Chapter 3 of our 2019 *Fiscal risks report*.
[27] Based on the average RBS share price over the ten days to 11 February, as with other market-derived assumptions in our forecast.

recorded in our March 2019 *EFO*. (The sharp fall in stock markets in the period since we closed our pre-measures forecast affected the RBS share price too, with the Government's shareholding on 6 March worth £11.8 billion.) The value of the Treasury's holdings in UKAR has risen slightly relative to last year to £8.9 billion (although this figure does not reflect UKAR's most recent repayments, so is likely to be revised down in its next set of accounts). If the Treasury were to receive all loan payments in full and to sell its remaining shares at their mid-February values, it would realise an overall cash surplus of £13.1 billion.

3.187 But the cash surplus estimate excludes the costs to the Treasury of financing these interventions. If all interventions are assumed to have been financed through gilts, at the then prevailing market rates, the Treasury estimates that the additional debt interest costs would have amounted to £40.0 billion by February, mainly due to the costs associated with RBS and UKAR.[28] This cost is larger than estimated last year, partly reflecting twelve more months servicing debt on interventions yet to be repaid or sold. Together this implies an overall cost of £26.9 billion to the Government (1.7 per cent of 2008-09 GDP), £0.4 billion less than we estimated last March.

## Table 3.39: Gross and net cash flows of financial sector interventions

| | £ billion | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Lloyds | RBS | UKAR[1] | FSCS[1] | CGS[1] | SLS[1] | Other | Total | Change since March 2019[2] |
| Cash outlays | -20.5 | -45.8 | -44.1 | -20.9 | 0.0 | 0.0 | -5.3 | -136.6 | 0.0 |
| Principal repayments | 21.1 | 6.3 | 43.7 | 20.9 | 0.0 | 0.0 | 5.3 | 97.3 | 2.3 |
| Other fees received[3] | 3.2 | 6.2 | 7.2 | 3.5 | 4.3 | 2.3 | 0.3 | 26.8 | 4.6 |
| Net cash position | 3.8 | -33.3 | 6.7 | 3.5 | 4.3 | 2.3 | 0.2 | -12.5 | 6.9 |
| Outstanding payments | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.1 | 0.1 | -2.3 |
| Market value[4] | 0.0 | 16.7 | 8.9 | 0.0 | 0.0 | 0.0 | 0.0 | 25.6 | -1.2 |
| Implied balance | 3.8 | -16.6 | 15.6 | 3.5 | 4.3 | 2.3 | 0.3 | 13.1 | 3.4 |
| Exchequer financing[5] | -4.2 | -15.5 | -13.0 | -8.3 | 1.3 | 0.3 | -0.6 | -40.0 | -3.0 |
| Overall balance | -0.4 | -32.1 | 2.6 | -4.8 | 5.5 | 2.6 | -0.2 | -26.9 | 0.4 |
| *Memo: changes in overall balance since March 2019*[2] | *-0.2* | *-1.2* | *2.2* | *-0.6* | *0.1* | *0.0* | *0.0* | *0.4* | |

[1] These are UK Asset Resolution (UKAR), which manages holdings in Bradford & Bingley and Northern Rock Asset Management plc., the Financial services compensation scheme (FSCS), Credit Guarantee Scheme (CGS), and Special Liquidity Scheme (SLS).
[2] March 2019 *EFO* figures were consistent with mid-February data.
[3] RBS figure contains fees related to the asset protection scheme and contingent capital facility. UKAR has dividends paid to the Treasury.
[4] UKAR is book value of equity, derived from its accounts as at 31 March 2019 published in June of that year.
[5] This can be split into financing while the intervention was open and after it closed (or after the final payment was received): Lloyds closed in May 2017, FSCS closed in October 2018, CGS closed in November 2012, and SLS closed in April 2012.

| | Lloyds | RBS | UKAR | FSCS | CGS | SLS | Other | Total |
|---|---|---|---|---|---|---|---|---|
| While open | -3.7 | -15.5 | -13.0 | -7.6 | 0.3 | 0.0 | -0.6 | -40.0 |
| After close | -0.5 | | | -0.7 | 1.0 | 0.3 | | 0.1 |

[28] The debt interest costs (or savings) associated with interventions that yield an overall deficit (or surplus) continue beyond the point the intervention itself has been wound up. This is the 'Exchequer financing' metric recorded in Table 3.39.

## Table 3.40: Fiscal aggregates

| | Per cent of GDP, unless otherwise stated | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Receipts and expenditure | | | | | | | |
| Public sector current receipts (a) | 37.5 | 37.7 | 37.9 | 38.0 | 38.3 | 38.4 | 38.5 |
| Total managed expenditure (b) | 39.3 | 39.8 | 40.3 | 40.8 | 40.8 | 40.8 | 40.7 |
| *of which:* | | | | | | | |
| Public sector current expenditure (c) | 35.0 | 35.3 | 35.4 | 35.7 | 35.6 | 35.5 | 35.4 |
| Public sector net investment (d) | 2.0 | 2.2 | 2.6 | 2.9 | 3.0 | 3.0 | 3.0 |
| Depreciation (e) | 2.3 | 2.2 | 2.3 | 2.3 | 2.3 | 2.3 | 2.3 |
| Legislated fiscal mandate and supplementary target | | | | | | | |
| Cyclically adjusted net borrowing | 1.9 | 2.2 | 2.4 | 3.0 | 2.7 | 2.5 | 2.2 |
| Public sector net debt[1] | 80.6 | 79.5 | 77.4 | 75.0 | 75.4 | 75.6 | 75.2 |
| Budget 2020 fiscal targets | | | | | | | |
| Current budget deficit (c+e-a) | -0.3 | -0.1 | -0.2 | -0.1 | -0.5 | -0.7 | -0.8 |
| Debt-interest-to-revenue ratio (per cent) | 4.1 | 3.8 | 3.3 | 3.5 | 3.3 | 3.1 | 2.9 |
| Other deficit measures | | | | | | | |
| Public sector net borrowing (b-a) | 1.8 | 2.1 | 2.4 | 2.8 | 2.5 | 2.4 | 2.2 |
| Cyclically adjusted current budget deficit | -0.1 | 0.0 | -0.2 | 0.1 | -0.2 | -0.5 | -0.8 |
| Primary deficit | 0.3 | 0.7 | 1.2 | 1.5 | 1.2 | 1.2 | 1.1 |
| Cyclically adjusted primary deficit | 0.4 | 0.8 | 1.2 | 1.7 | 1.5 | 1.3 | 1.1 |
| Financing | | | | | | | |
| Central government net cash requirement | 2.4 | 2.0 | 2.8 | 3.1 | 2.8 | 2.5 | 2.7 |
| Public sector net cash requirement | 2.1 | 1.4 | 1.1 | 0.3 | 2.9 | 2.6 | 2.7 |
| Alternative balance sheet metrics | | | | | | | |
| Public sector net debt ex. Bank of England | 72.3 | 71.9 | 71.9 | 72.3 | 72.9 | 73.1 | 72.9 |
| Public sector net financial liabilities | 67.4 | 66.7 | 65.9 | 65.3 | 64.9 | 64.5 | 63.4 |
| Stability and Growth Pact | | | | | | | |
| Treaty deficit[2] | 1.8 | 2.2 | 2.5 | 3.1 | 2.6 | 2.4 | 2.4 |
| Cyclically adjusted Treaty deficit | 1.9 | 2.3 | 2.5 | 3.3 | 2.8 | 2.5 | 2.4 |
| Treaty debt ratio[3] | 84.1 | 83.2 | 82.9 | 83.2 | 83.3 | 83.3 | 83.0 |
| | £ billion | | | | | | |
| Current budget deficit | -5.8 | -1.7 | -4.9 | -2.7 | -11.7 | -16.7 | -21.2 |
| Public sector net investment | 44.3 | 49.1 | 59.7 | 69.3 | 73.2 | 77.0 | 79.1 |
| Public sector net borrowing | 38.4 | 47.4 | 54.8 | 66.7 | 61.5 | 60.2 | 57.9 |
| Cyclically adjusted net borrowing | 41.4 | 48.2 | 55.3 | 71.8 | 68.1 | 63.9 | 58.7 |
| Cyclically adjusted current budget deficit | -2.8 | -1.0 | -4.4 | 2.5 | -5.1 | -13.1 | -20.4 |
| Public sector net debt | 1774 | 1799 | 1818 | 1827 | 1900 | 1969 | 2031 |
| Net debt interest | 32.5 | 30.9 | 28.1 | 31.2 | 30.6 | 29.3 | 28.5 |
| Non-interest receipts | 788.9 | 811.8 | 845.3 | 881.9 | 918.6 | 952.3 | 988.4 |
| *Memo: Output gap (per cent of GDP)* | *0.3* | *0.0* | *0.1* | *0.4* | *0.4* | *0.1* | *0.0* |

[1] Debt at end October; GDP centred on end October.
[2] General government net borrowing.
[3] General government gross debt. Uses financial year GDP.

## Risks, uncertainties and contingent liabilities

### Risks and uncertainties

3.188 We always emphasise the uncertainties that lie around our central fiscal forecast. For example, those around the UK's future trading relationship with the EU and the economic and fiscal effects of the new migration regime. But unusually in this forecast it is already clear that downside risks predominate as coronavirus spreads, with negative implications for the economy and public finances that are impossible to quantify reliably at this stage.

3.189 As usual, we have exposed our judgements to various sensitivities in Chapter 4, although not the presently unquantifiable risks posed by coronavirus. Several of the risks we highlighted in our 2019 *FRR* remain key sources of uncertainty too:

- Macroeconomic risks: such as risks to potential output growth from productivity and migratory flows and the cyclical risks that the economy falls into recession at some point in the next five years – quite possibly this year if some predictions for the possible effects of coronavirus were to be realised, causing widespread economic disruption.

- Financial sector risks: the UK remains home to one of the world's largest financial sectors, both in absolute terms and relative to the size of the economy. The fiscal risks that can be associated with this have been illustrated clearly over the past 15 years.

- Revenue-specific risks: we highlighted potential pressures on the sustainability of various tax bases. In recent forecasts, we have seen several near-term upside surprises, some of which have already been partly reversed. Asset prices have fallen sharply since we closed our forecast, which would hit capital tax receipts if they were to persist. The policy-related risks we have previously highlighted – such as the continued year-by-year freezing of duties on fuel – have crystallised yet again in this forecast.

- Primary spending risks (i.e. spending on everything other than debt interest): the fiscal policy response to coronavirus could raise public spending materially in the short term to address the crisis, but may also limit the Government's ability to ramp up capital spending as quickly as it hopes. The scale and persistence of any spending rise will of course depend on the severity of the effects in the UK. These costs will come on top of other pressures that have not gone away – notably long-term pressures in health care and pensions. The 'austerity fatigue' risks we noted in the *FRR* have crystallised in this Budget with the multi-billion increases in departmental spending plans.

- Balance sheet risks: these can relate to real-world events or statistical changes. In this forecast, risks to our debt forecast from delays to asset sales have partly crystallised through further delays in sales of RBS shares and the cancellation of student loans sales (the latter increases our debt forecast but improves broader balance sheet measures). We have also highlighted the potential changes in the treatment of leases and of Pool Re, a terrorism reinsurer, as potential sources of risk to the forecast.

- Debt interest risks: in the *FRR* we discussed the risks associated with the 'growth-corrected interest rate' – i.e. the gap between interest rates and economic growth, which influences the path of debt relative to GDP. We noted the historically favourable position at present, but also the risks to it given the extent and persistence of past variations. The Government has pointed to historically low interest rates as a reason to be content with a broadly flat debt-to-GDP ratio in the medium term. This starting position could pose risks if interest rates were to rise relative to GDP growth.

## Comparison to the pre-crisis picture

3.190 The Government's new fiscal plans in some ways resemble those of the Labour Government ahead of the financial crisis in the late 2000s. Both seek to balance the current budget and sustain higher public investment, leaving borrowing relatively high and the debt-to-GDP ratio broadly stable. As Chart 3.14 shows:

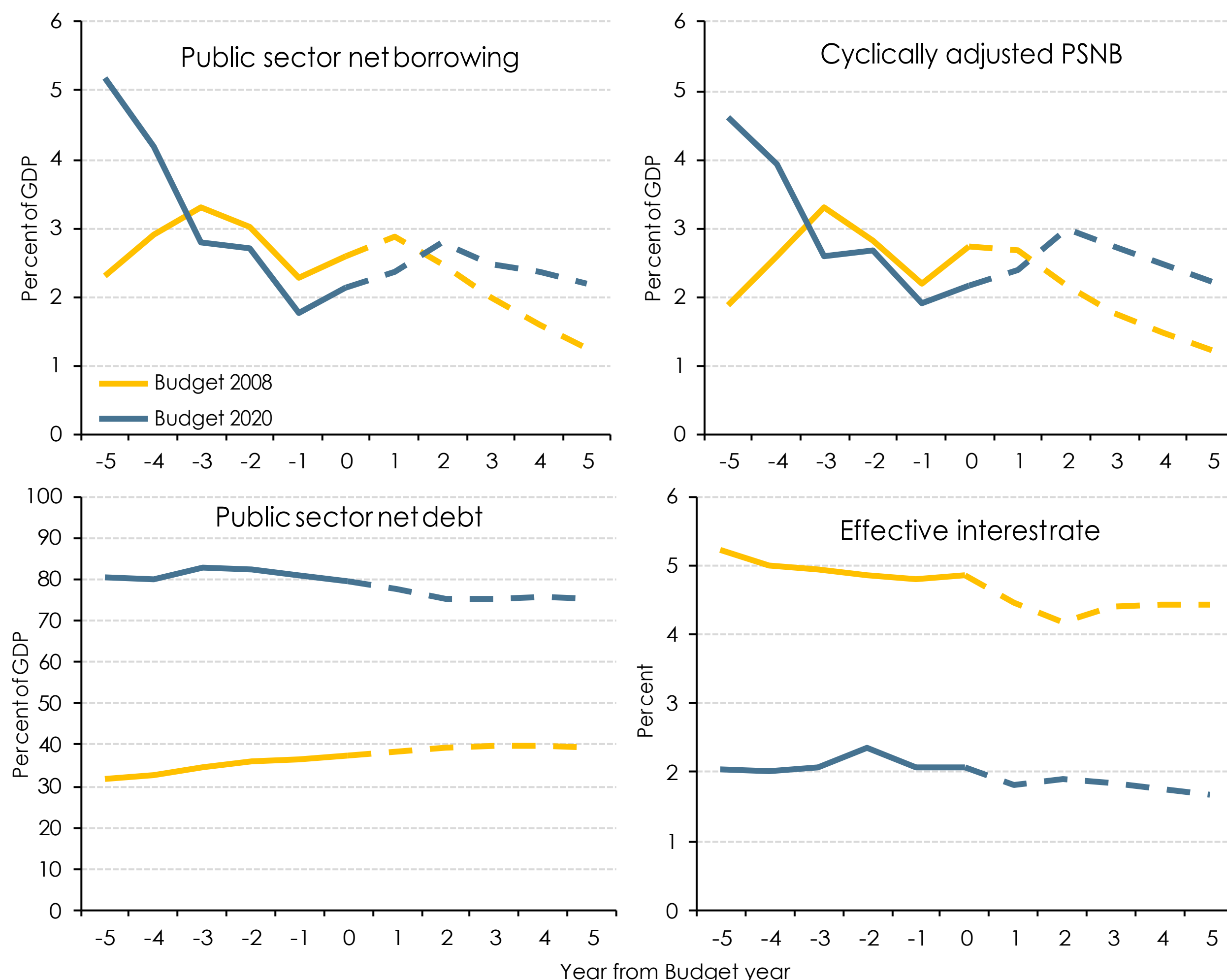
- The headline deficit (PSNB) averages 2.4 per cent of GDP in the five years from 2020-21 to 2024-25, which compares with 2.0 per cent in the five years from 2008-09 to 2012-13 that was predicted in Budget 2008 and the 2.8 per cent of GDP that it had averaged between 2003-04 and 2007-08.

- The structural deficit (cyclically adjusted PSNB) averages 2.6 per cent of GDP over that period, compared with 1.9 per cent over the equivalent period in Budget 2008 and 2.7 per cent in the five years preceding that Budget.

- The debt-to-GDP ratio ends the forecast 4.3 per cent of GDP lower than it starts it, which compares with the 2.2 per cent of GDP rise expected in Budget 2008. But the level of debt is much higher now – 75.2 per cent of GDP by 2024-25 versus just 39.3 per cent of GDP at the Budget 2008 forecast horizon.

- Both forecasts assumed that interest rates would remain broadly stable, with the effective interest rate paid on government debt falling by 0.4 percentage points between 2019-20 and 2024-25 in our latest forecast and by the same amount over the Budget 2008 forecast horizon. But the level of interest rates is much lower now than it was then, with the effective rate expected to be just 1.7 per cent in 2024-25 versus 4.4 per cent at the Budget 2008 horizon.

## Chart 3.14: The fiscal outlook: Budget 2020 versus Budget 2008

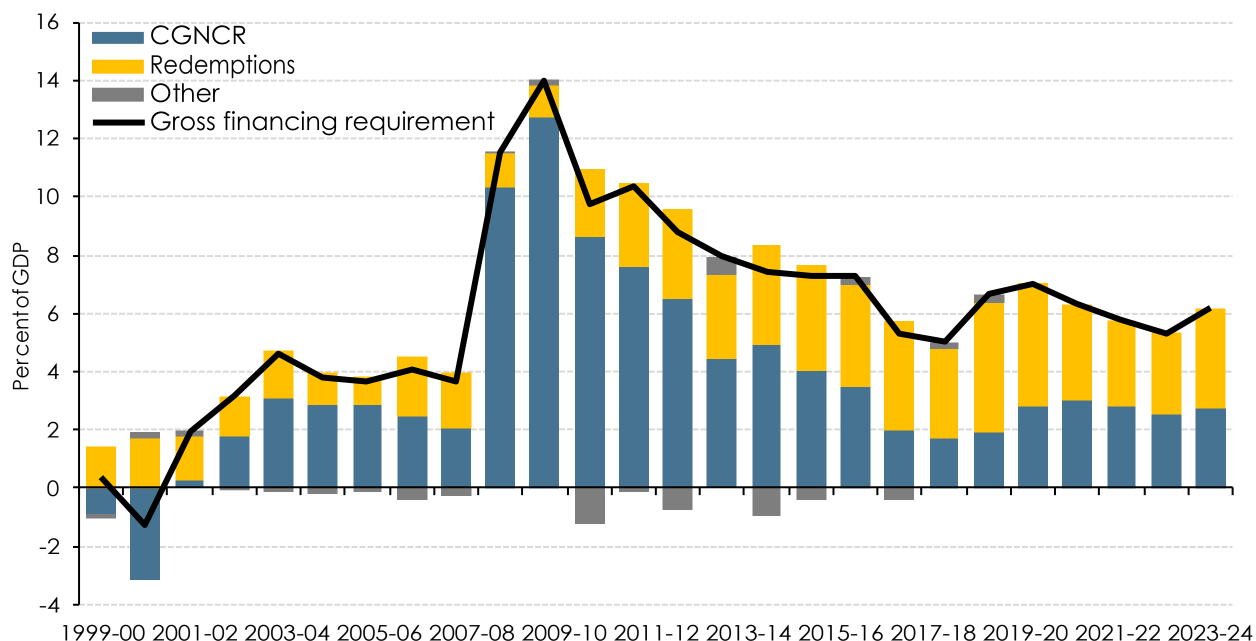



Note: Effective interest rate definied as CG debt interest (net of APF) divided by GG gross debt.
Source: HM Treasury, OBR

3.191 The current Government's fiscal plans are rooted in the assumption that its borrowing costs will remain relatively low, as market expectations indeed suggest. Rather than aim for a balanced budget overall and a significant decline in the debt-to-GDP ratio – as Philip Hammond did initially as Chancellor – the new administration is content to borrow significant sums on an ongoing basis and merely to stabilise the debt-to-GDP ratio.

3.192 This looks sustainable over the medium term on current interest rate and growth forecasts. But, as we have noted in our *Fiscal risks reports*, financing conditions may not remain this favourable. The debt-to-GDP is twice as high as in the pre-crisis period, the stock of index-linked gilts is much larger and the Bank of England's asset purchases have shortened the effective maturity of public debt. Taking both fresh borrowing and the need to roll over existing debt into account, the Government's gross financing requirement averages around 6 per cent of GDP a year over the next five years, around half as high again as in the five years prior to the crisis (Chart 3.15). So the public finances are much more vulnerable to inflation and interest rate surprises than they were.

## Chart 3.15: Gross financing requirement




Source: DMO, OBR

## Contingent liabilities

3.193 We have as usual asked the Treasury to identify any changes to future contingent liabilities since our March 2019 forecast. Its dedicated reporting system records 32 that were entered into over that period or that are soon to be entered into, with a total maximum exposure of £32.4 billion for those that have been quantified. We judge that overall these do not materially affect risks to the public finances as the chance of them crystallising seems generally quite remote.

3.194 In December 2018 the Court of Appeal ruled that the transitional protection offered to some members of the judges' and firefighters' pensions schemes, as part of the wider public sector pensions reforms, gave rise to unlawful age discrimination (the McCloud and Sargeant cases). On 15 July 2019 the Government confirmed to Parliament that the difference in treatment will be remedied across all the main schemes – including NHS, civil service, police – but it has not outlined the final policy. The Treasury's initial estimate suggested that remedying the discrimination would add around £4 billion a year to scheme liabilities from 2015. The Government has not yet included cash impacts in the schemes' AME spending forecasts, nor made allowances in departmental budgets.

3.195 A legal process initiated by the European Commission represents a source of risk to our fiscal forecast. It regards the UK's application of a zero rate of VAT to certain derivative transactions. The Commission has now referred the UK to the European Court of Justice.

# 4 Performance against the Government's fiscal targets

## Introduction

4.1 This chapter:

- sets out the current legislated fiscal targets and assesses the chances of them being met on current policy, given our central forecast (from paragraph 4.4);
- describes the fiscal targets that have guided the Government's policy decisions in this Budget, and assesses the chances of meeting them (from paragraph 4.15); and
- assesses how robust these judgements are to the uncertainties inherent in any fiscal forecast, by looking at past differences between forecast and outturn, sensitivity to key parameters of the forecast, and alternative scenarios (from paragraph 4.27).

4.2 As set out in Chapters 2 and 3, in the period between closing these forecasts and publishing them, it has become clear that the coronavirus outbreak is likely to have a more adverse effect on the UK economy and public finances than appeared likely a few weeks ago. There is still value in assessing performance against the targets thoroughly, however, since it shows how the Government chose to set fiscal policy given the pre-measures forecasts that we presented. But it is also clear that the near-term risks to those forecasts are to the downside. The legislated fiscal targets are particularly vulnerable since they apply in 2020-21. The extent to which performance against the new targets might be affected is less clear.

4.3 The *Charter for Budget Responsibility* requires the OBR to judge whether the Government has a greater than 50 per cent chance of meeting each of its fiscal targets under current policy. The *Charter* has been updated several times as governments have revised these targets and the latest version approved by Parliament is from January 2017.[1] The policy decisions in this Budget have been guided not by the *Charter*, but by the targets that were set out in the Conservative Party manifesto and confirmed in the Queen's Speech (and that are described in the next section). The Government intends to review the fiscal framework ahead of the next Budget in the autumn, so the targets could change again.

[1] The latest and previous versions are available on the 'Legislation and related material' page of our website.

## The legislated fiscal targets

4.4 The current *Charter* says that the Government's objective for fiscal policy is to "*return the public finances to balance at the earliest possible date in the next Parliament*". At the time this was drawn up, 'the next Parliament' was expected to run from 2020 to 2025. The *Charter* also sets: a 'fiscal mandate' that requires *the structural deficit* (cyclically adjusted public sector net borrowing) to lie below 2 per cent of GDP by 2020-21; a 'supplementary target' that requires *public sector net debt* to fall relative to GDP in 2020-21; and a requirement for a subset of welfare spending to lie below an effective 'welfare cap' of £135 billion in 2022-23, with the cap adjusted for subsequent changes in our inflation forecast.

## The implications of our central forecast

4.5 Table 4.1 shows our central forecasts for the aggregates relevant to the legislated fiscal targets and objective: cyclically adjusted public sector net borrowing (PSNB); public sector net debt (PSND); spending subject to the welfare cap; and headline PSNB. These are described in Chapter 3. They should be interpreted as median forecasts, so outturns are as likely to come in above them as below them. But they are also conditional forecasts – they reflect current stated government policy (as Parliament requires), rather than how we might expect policy to evolve. And, more importantly for this forecast, they reflect pre-measures forecasts and conditioning assumptions that date from mid-February.

### Table 4.1: Forecasts for the Government's current target aggregates

| | Per cent of GDP, unless otherwise stated | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Fiscal mandate: Cyclically adjusted public sector net borrowing in 2020-21 | | | | | | | |
| March 2019 forecast | 1.2 | 1.3 | 0.8 | 0.7 | 0.6 | 0.5 | |
| Restated March 2019 forecast | 2.0 | 2.1 | 1.7 | 1.5 | 1.4 | 1.3 | |
| March 2020 pre-measures forecast | 1.9 | 2.2 | 1.8 | 1.7 | 1.5 | 1.3 | 1.1 |
| March 2020 post-measures forecast | 1.9 | 2.2 | 2.4 | 3.0 | 2.7 | 2.5 | 2.2 |
| Supplementary target: Year-on-year change in public sector net debt in 2020-21 | | | | | | | |
| March 2019 forecast | 83.3 | 82.2 | 79.0 | 74.9 | 74.0 | 73.0 | |
| Restated March 2019 forecast | 82.2 | 81.3 | 78.2 | 74.3 | 73.6 | 72.7 | |
| March 2020 pre-measures forecast | 80.6 | 79.2 | 76.9 | 73.6 | 73.0 | 72.0 | 70.8 |
| March 2020 post-measures forecast | 80.6 | 79.5 | 77.4 | 75.0 | 75.4 | 75.6 | 75.2 |
| Welfare cap: Specified welfare spending in 2022-23 (£ billion) | | | | | | | |
| March 2019 forecast | 119.3 | 121.4 | 123.2 | 126.0 | 129.5 | 133.7 | |
| Restated March 2019 forecast | 119.3 | 121.4 | 123.2 | 126.0 | 129.5 | 133.7 | |
| March 2020 pre-measures forecast | 119.5 | 121.7 | 125.7 | 128.1 | 131.5 | 135.5 | 138.8 |
| March 2020 post-measures forecast | 119.5 | 119.0 | 122.6 | 124.3 | 127.0 | 130.2 | 133.5 |
| Fiscal objective: Public sector net borrowing up to 2025-26 | | | | | | | |
| March 2019 forecast | 1.1 | 1.3 | 0.9 | 0.7 | 0.6 | 0.5 | |
| Restated March 2019 forecast | 1.9 | 2.2 | 1.8 | 1.6 | 1.5 | 1.3 | |
| March 2020 pre-measures forecast | 1.8 | 2.2 | 1.9 | 1.8 | 1.6 | 1.4 | 1.1 |
| March 2020 post-measures forecast | 1.8 | 2.1 | 2.4 | 2.8 | 2.5 | 2.4 | 2.2 |

4.6 Table 4.2 summarises expected performance against the legislated fiscal targets in the years in which they apply, and how the margins by which we expect them to be met (or not) have changed since March 2019. The rest of this section sets out the assessments we make based on these figures and the reasons for the changes observed since March 2019.

## Table 4.2: Performance against the Government's current fiscal and welfare targets

| | | Per cent of GDP | | £ billion | |
|---|---|---|---|---|---|
| | | Forecast | Margin | Forecast | Margin |
| **Fiscal mandate: Cyclically adjusted public sector net borrowing in 2020-21** | | | | | |
| March 2019 forecast | Met | 0.8 | 1.2 | 18.9 | 26.6 |
| Restated March 2019 forecast | Met | 1.7 | 0.3 | 37.9 | 7.6 |
| March 2020 pre-measures forecast | Met | 1.8 | 0.2 | 40.5 | 5.3 |
| March 2020 post-measures forecast | Not met | 2.4 | -0.4 | 55.3 | -9.2 |
| *Memo: Overall change since March 2019* | | *1.6* | *-1.6* | *36.5* | *-35.9* |
| **Supplementary target: Year-on-year change in public sector net debt in 2020-21** | | | | | |
| March 2019 forecast | Met | -3.2 | 3.2 | | |
| Restated March 2019 forecast | Met | -3.1 | 3.1 | | |
| March 2020 pre-measures forecast | Met | -2.3 | 2.3 | | |
| March 2020 post-measures forecast | Met | -2.1 | 2.1 | | |
| *Memo: Overall change since March 2019* | | *1.2* | *-1.2* | | |
| **Welfare cap: Specified welfare spending in 2022-23** | | | | | |
| March 2019 forecast | Met | | | 129.5 | 5.5 |
| Restated March 2019 forecast | Met | | | 129.5 | 5.5 |
| March 2020 pre-measures forecast | Met | | | 131.5 | 2.1 |
| March 2020 post-measures forecast | Met | | | 127.0 | 3.4 |
| *Memo: Overall change since March 2019* | | | | *-2.5* | *-2.1* |

### The legislated fiscal mandate

4.7 The legislated fiscal mandate requires the structural deficit to lie below 2 per cent of GDP by 2020-21. Our forecast shows this being missed by 0.4 per cent of GDP, having been met in our March 2019 forecast with 1.2 per cent of GDP to spare. This reflects:

- Statistical changes and corrections incorporated by the ONS in its September 2019 public sector finance release and reflected in our restated March 2019 forecast. These reduced the margin from 1.2 to 0.3 per cent of GDP (£26.6 billion to £7.6 billion). The change was dominated by the new accounting treatment of student loans (adding £14.1 billion) and a correction to corporation tax receipts (adding £4.3 billion).

- Pre-measures forecast changes decrease the margin slightly further to 0.2 per cent of GDP (£5.3 billion), thanks largely to higher capital spending.

- Budget policy measures and other Government decisions announced since March 2019 add 0.6 per cent of GDP (£14.8 billion) to cyclically adjusted PSNB in 2020-21, leaving the fiscal mandate missed by 0.4 per cent of GDP (£9.2 billion). This is dominated by the higher spending announced in the 2019 Spending Round.

## The legislated supplementary debt target

4.8 The legislated supplementary debt target requires PSND to fall relative to GDP in 2020-21. Based on our central forecast, it falls by 2.1 per cent of GDP in 2020-21, down from the 3.2 per cent margin in March 2019. The margin was little changed by the statistical changes incorporated in our restated forecast, as they mostly related to accrued receipts and spending while leaving the cashflows that drive PSND largely unaffected. The downward revision to our pre-measures forecast for nominal GDP growth modestly reduced the margin by which the target is met. Government decisions have reduced it further, thanks largely to higher spending – the effect of which is partly offset by the indirect effects of that fiscal easing on our post-measures forecast for nominal GDP growth.

4.9 Our forecast assumes that repayment of loans issued under the Bank of England's Term Funding Scheme during 2020-21 will lower PSND by £43.7 billion, reducing the PSND-to-GDP ratio by 1.9 percentage points relative to 2019-20. So, absent these repayments, PSND would fall by just 0.2 per cent of GDP in the target year.

## The welfare cap

4.10 Table 4.3 shows our latest forecast for spending subject to the welfare cap and how it compares with the cap, pathway and margin as they stood in our March 2019 forecast. As this is the first forecast of a new Parliament, this represents our formal assessment of the Government's performance against the cap. The welfare cap has been reset at this Budget in line with our latest forecast. We have revised spending up since the cap was last reset, in November 2017, leaving it above the cap and the pathway to it from 2020-21 onwards. But the terms of the target have nonetheless been met, with spending below the cap *plus margin* in all years, with or without small adjustments for revisions to our inflation forecast.[2]

[2] The *Charter* requires revisions to our inflation forecast since November 2017 to be stripped out using a methodology set by the Treasury.

## Table 4.3: Performance against the current welfare cap

| | £ billion, unless otherwise stated | | | |
|---|---|---|---|---|
| | Forecast | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 |
| Welfare cap | | | | 131.1 |
| Pathway | 122.0 | 124.7 | 127.8 | |
| Margin (per cent) | 1.5 | 2.0 | 2.5 | 3.0 |
| Margin | 1.8 | 2.5 | 3.2 | 3.9 |
| Welfare cap and pathway plus margin | 123.8 | 127.2 | 131.0 | 135.0 |
| Latest forecast and update on performance against cap and pathway | | | | |
| March 2020 forecast | 119.0 | 122.6 | 124.3 | 127.0 |
| Inflation adjustment | -0.1 | +0.0 | +1.0 | +1.1 |
| Scottish welfare block grant adjustment | +0.3 | +3.1 | +3.3 | +3.4 |
| March 2020 forecast after adjustments | 119.2 | 125.8 | 128.5 | 131.6 |
| *Difference from:* | | | | |
| Cap and pathway | -2.8 | +1.1 | +0.7 | +0.5 |
| Cap and pathway plus margin | -4.6 | -1.4 | -2.5 | -3.4 |
| *Memo: cumulative percentage point change in preceding September (Q3) rates of inflation since our November 2017 forecast.* | *0.4* | *0.4* | *-0.4* | *-0.5* |

Note: The inflation adjustment is negative for 2019-20 and positive for future years as inflation is higher in 2019-20 than forecast in our November 2017 *EFO* and then lower for the rest of the forecast. This takes the effect of the change in inflaton out of the spending forecast.

4.11 As this is the first Budget of a new Parliament, the *Charter* requires the Government to set a new cap. The Government has retained the approach in Autumn Budget 2017 of setting a cap and pathway in line with our latest forecast and applying a progressively larger margin above it to set the effective cap. The new cap is higher than the one it replaces.

## Table 4.4: The new welfare cap and margin

| | £ billion | | | | | |
|---|---|---|---|---|---|---|
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Welfare cap | | | | | | 137.2 |
| Pathway | 119.3 | 125.7 | 127.5 | 130.5 | 133.8 | |
| Margin (per cent) | 0.5 | 1.0 | 1.5 | 2.0 | 2.5 | 3.0 |
| Margin | 0.6 | 1.3 | 1.9 | 2.6 | 3.3 | 4.1 |
| Welfare cap and pathway plus margin | 119.9 | 127.0 | 129.5 | 133.1 | 137.1 | 141.3 |

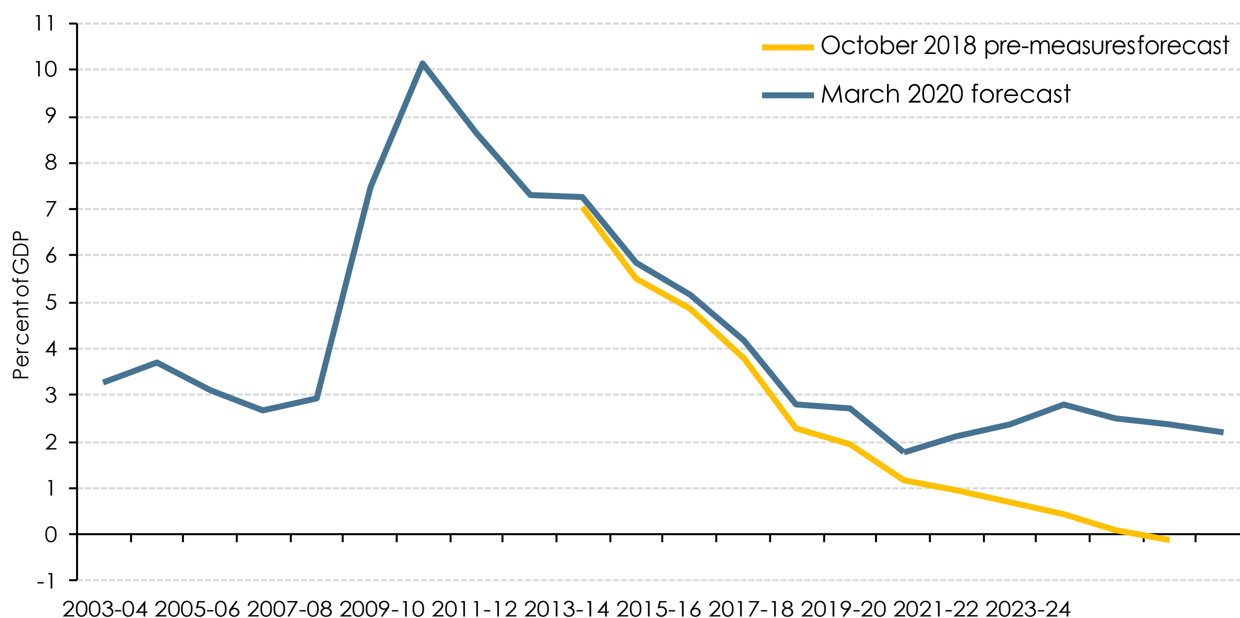
### The legislated fiscal objective

4.12 The current *Charter* states that the Government's fiscal objective is to "*return the public finances to balance at the earliest possible date in the next Parliament*". When this objective was set in November 2016, the 'next Parliament' was expected to run to May 2025, so the 'earliest possible date' could have been anywhere up to 2025-26. In the event, there have already been two elections since. Our forecast horizon extends to 2024-25, so we cannot assess performance against this objective definitively using a central forecast for 2025-26.

4.13 A year and a half ago, the pre-measures forecast in our October 2018 *Economic and fiscal outlook (EFO)* showed the Government on course to balance the budget and thus meet the fiscal objective ahead of schedule in 2023-24 – with a £3.5 billion surplus projected for that

year (Chart 4.1). By contrast, this forecast shows a projected deficit of £60.2 billion (2.4 per cent of GDP) for that year. The deficit is forecast to drop to 2.2 per cent of GDP in 2024-25, but thereafter will face upward pressure on spending from an ageing population and from cost pressures in health and adult social care spending.

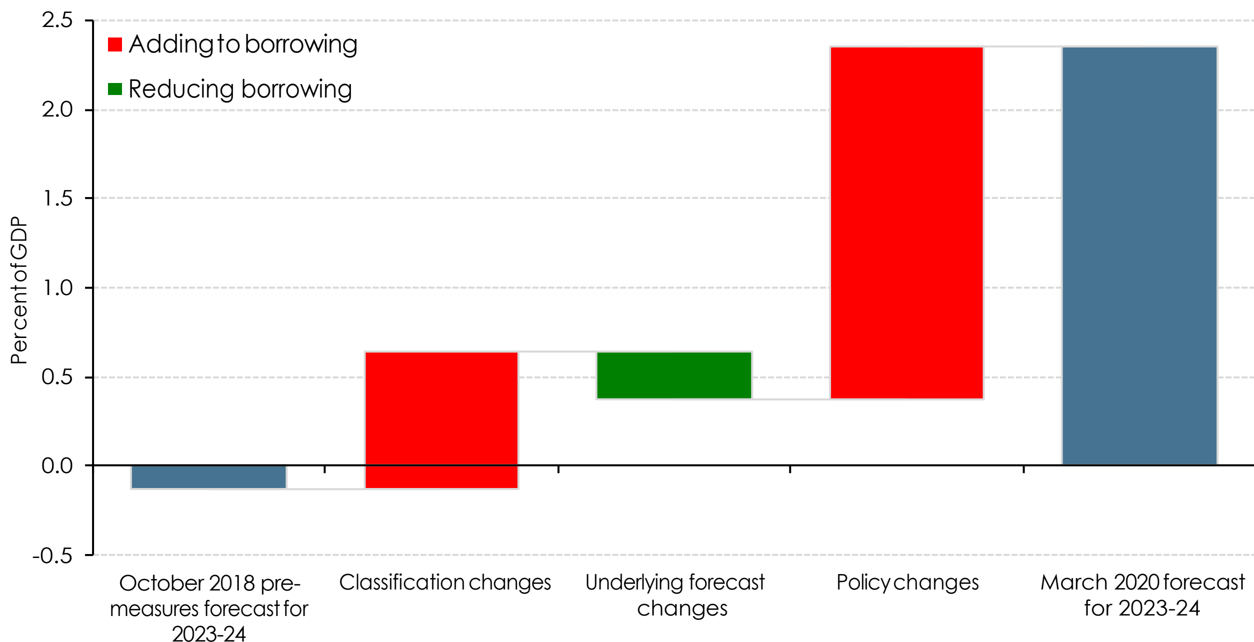
## Chart 4.1: Public sector net borrowing




Source: ONS, OBR

4.14 As Chart 4.2 shows, the 2.5 per cent of GDP increase in our forecast for the deficit in 2023-24 since the October 2018 pre-measures forecast reflects: 0.8 per cent of GDP of classification changes (mostly the new treatment of student loans); a 0.3 per cent of GDP improvement in the underlying forecast; and a cumulative policy loosening of 2.0 per cent of GDP over the past three fiscal events, as the objective was rhetorically (if not legally) downplayed and then abandoned.

## Chart 4.2: Change in net borrowing in 2023-24




Source: OBR

# The Budget 2020 fiscal targets

## Definitions of the Budget 2020 targets

4.15 The Government has informed us that its policy decisions in this Budget have been guided by the fiscal rules set out in the Conservative manifesto that were confirmed in the Queen's Speech in January. It has asked us to assess performance against these rules. The Chancellor does not intend to legislate for these rules at this Budget by laying a revised *Charter for Budget Responsibility*, but will instead review the fiscal framework ahead of the Autumn Budget. In his letter, the Chancellor defines the fiscal rules as:

- to have the current budget at least in balance by the third year of the rolling five-year forecast period;
- to ensure that public sector net investment does not exceed 3 per cent of GDP on average over the rolling five-year forecast period; and
- if the debt-interest-to-revenue ratio is forecast to remain over 6 per cent for a sustained period, the Government will act to ensure the debt-to-GDP ratio is falling.

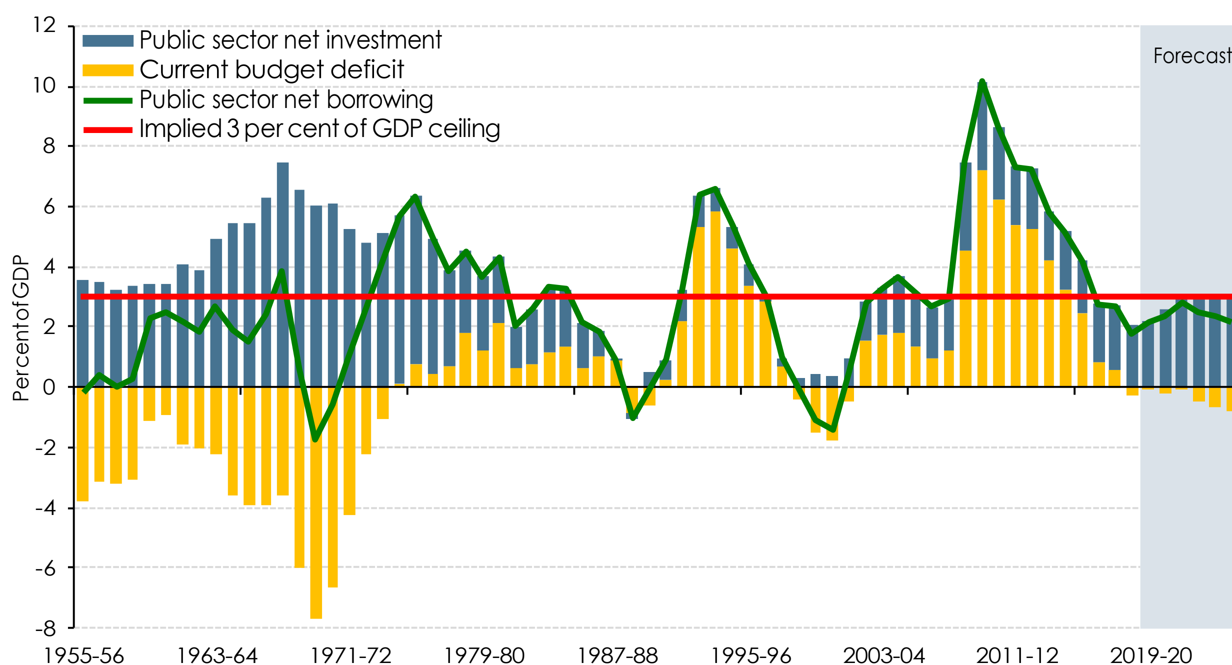
He defines the debt-interest-to-revenue ratio as public sector net interest paid (i.e. gross interest paid less interest received) as a proportion of non-interest receipts.

4.16 For most of the past quarter of a century, the main 'flow' fiscal target in the UK has related to the current budget balance – notably Labour's 'golden rule' from 1997 to 2008 and the Coalition's 'fiscal mandate' from 2010 to 2015. So the target for the current budget is a

return to familiar ground. But flow targets have typically been accompanied by a stock target: Labour had a 'sustainable investment rule' that public sector net debt should not exceed 40 per cent of GDP; the Coalition had a 'supplementary debt target' stipulating the year by which debt should start falling as a share of GDP. Instead of a stock target, the Budget 2020 rules place a ceiling on the flow of investment relative to GDP (a 'maximum investment rule') and interest payments relative to receipts (the 'debt-interest-to-revenue ratio rule'), but their only mention of the level or path of debt is in specifying that the Government will act to ensure the debt-to-GDP ratio falls if the debt-interest-to-revenue ratio exceeds 6 per cent on a sustained basis.

4.17 As Chart 4.3 shows, PSNB has averaged 2.9 per cent of GDP since 1955, but has exceeded 3 per cent of GDP in 28 out of those 64 years. The deficit topped 6 per cent of GDP during the 1973 oil crisis, the ERM crisis of the early 1990s and the financial crisis of the late 2000s. In each case it remained well above 3 per cent of GDP for some years afterwards. Up to the mid-1970s, high levels of public investment were consistently offset by current budget surpluses, mostly keeping the overall deficit below 3 per cent of GDP.

## Chart 4.3: Public sector net borrowing and the implied 3 per cent ceiling




Source: ONS, OBR

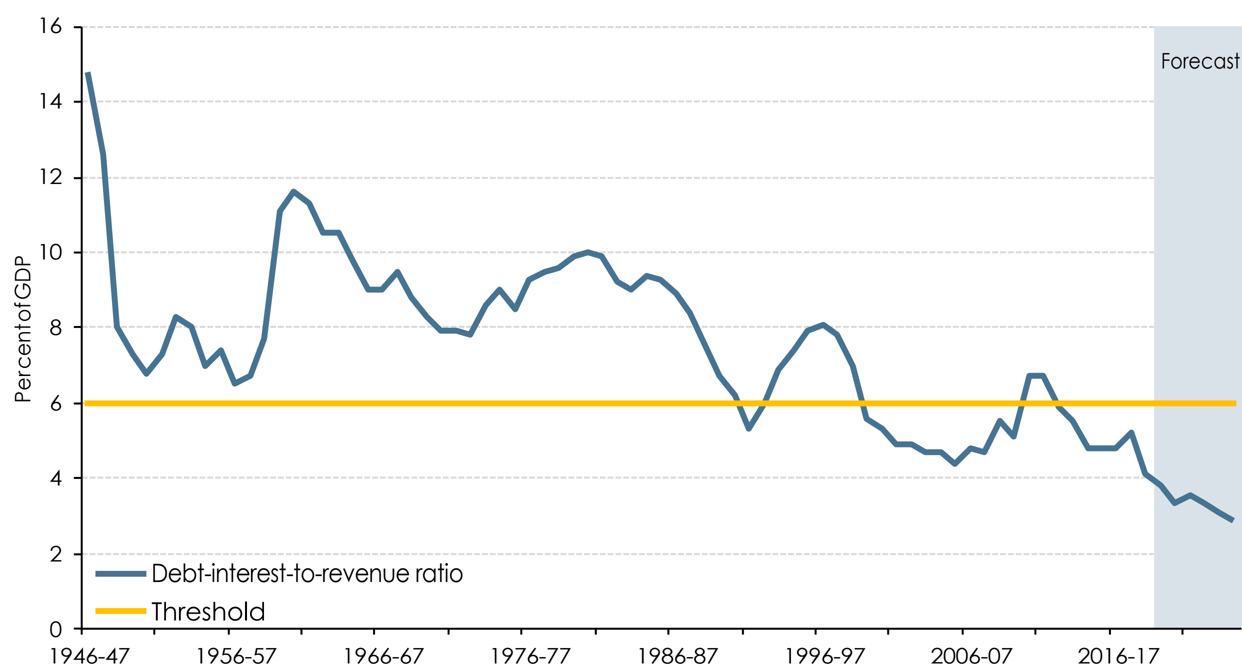
## What do these rules mean for fiscal sustainability?

4.18 Relative to the legislated targets, the rules adopted for this Budget are materially looser. They require the current budget to be in balance by the third year of the forecast (2022-23 in this one) and public sector net investment (PSNI) not to exceed 3 per cent of GDP. This puts a ceiling of 3 per cent of GDP on the deficit and affords 1 per cent of GDP more space than the legislated deficit rule (£22.3 billion in today's terms) and 3 per cent of GDP more than the legislated fiscal objective (£66.9 billion). A new debt-interest-to-revenue ratio rule requires net interest costs to be less than 6 per cent of primary (i.e. non-interest) receipts.

4.19 The Conservative manifesto stated that the pursuit of these targets "*means that debt will be lower at the end of the Parliament*". But observing these rules does not mean that debt will always fall relative to GDP. As well as borrowing, the path of debt depends on two other factors: the net cost of financial transactions (which are not covered by the rules) and the rate of nominal GDP growth (over which inflation-targeting governments have little control). Given our medium-term expectations for these variables, the maximum deficit consistent with a stable debt-to-GDP ratio is around 2.5 per cent of GDP. So the Chancellor would need to over-achieve his new rules on average to ensure that debt falls in normal times.

4.20 As Chart 4.4 shows, until 1990-91 the debt interest to revenue ratio was above 6 per cent every year, reflecting much higher interest rates on government debt than is the case now and, initially, the very high post-war debt-to-GDP ratio. But the debt ratio fell through most of this period as the high interest rates were usually accompanied by high nominal GDP growth. This illustrates that a high debt interest to revenue ratio does not guarantee rising debt. Neither does a low ratio necessarily lead to debt falling – the ratio was 4.7 per cent in 2007-08 ahead of the financial crisis and only exceeded 6 per cent twice over the subsequent decade (in 2010-11 and 2011-12 thanks to spikes in RPI inflation), despite the debt-to-GDP ratio rising from 34.2 to 82.4 per cent over that period.

## Chart 4.4: The debt interest to revenue ratio




Source: ONS, OBR

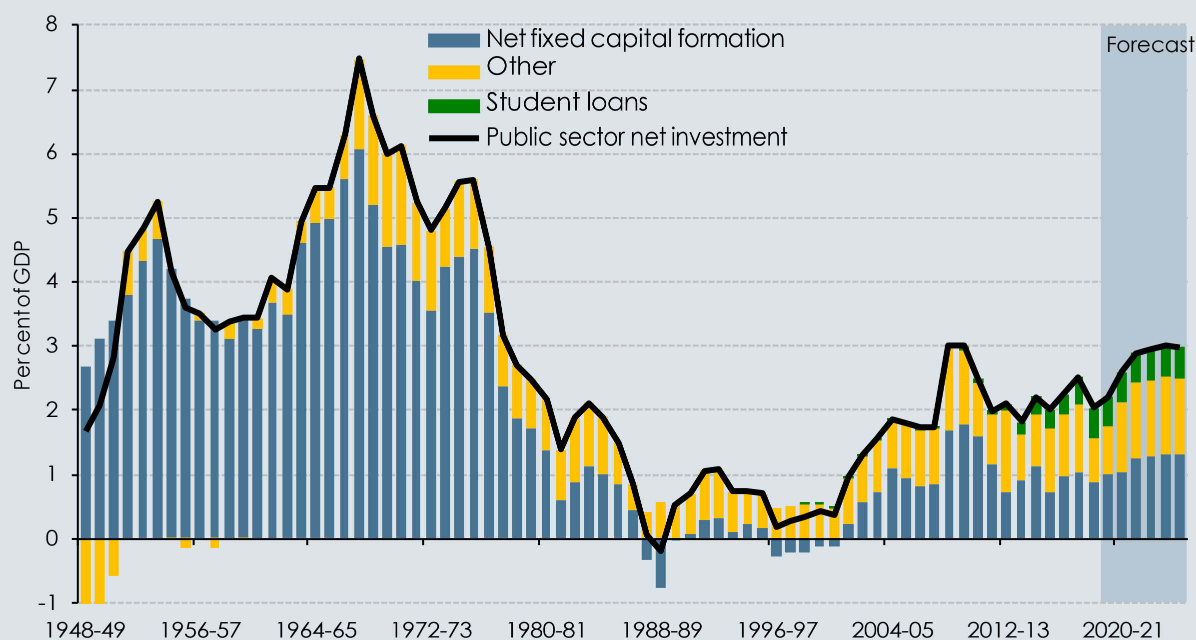
## Box 4.1: Public sector net investment

Public sector net investment (PSNI) consists of three main elements:

- The largest – gross fixed capital formation (GFCF) – is what is normally thought of as capital spending. It is the net acquisition of fixed assets (such as roads, buildings and weapons systems) by the public sector, as well as a significant amount of R&D spending.
- The depreciation of these assets forms the second largest component and is negative.
- The remainder consists almost entirely of capital grants to and from the private sector. Some of these – for example grants for social housing – will be used to increase fixed assets in the private sector. Others – such as upfront recognition of student loan write-offs and the net assumption of pension liabilities by the Pension Protection Fund – will not.

Taken together GFCF minus depreciation (net fixed capital formation, NFCF) represents the cash increase in the public sector's net capital stock. As Chart A shows, NFCF averaged around 4 per cent of GDP up to the 1970s, when the public sector included some major industries and investment in public housebuilding was much higher than it is today. It was much smaller, and occasionally negative, over the next two decades – when industries and much social housing left the public sector – before picking up to around 1 per cent of GDP on average so far this century. Government plans will lift NFCF to 1.2 per cent of GDP over the forecast. At an average of 1.6 per cent of GDP, capital grants are larger than NFCF over the forecast period (with capital transfers associated with student loan outlays reaching 0.5 per cent of GDP in 2024-25).

### Chart A: Historical trends in public sector net investment



Source: ONS, OBR

## The implications of our central forecast

4.21 Table 4.5 shows our central forecasts for the fiscal aggregates relevant to the Budget 2020 fiscal targets: the current budget deficit; PSNI; the net debt interest to primary revenue ratio; and spending subject to the welfare cap. Table 4.6 summarises performance against these targets and the margins by which they are forecast to be met.

### Table 4.5: Forecasts for the Budget 2020 target aggregates

| | Per cent of GDP, unless otherwise stated | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Current budget rule: Current budget balanced by 2022-23[1] | | | | | | | |
| March 2020 pre-measures forecast | -0.3 | -0.2 | -0.6 | -0.6 | -0.8 | -1.0 | -1.3 |
| March 2020 post-measures forecast | -0.3 | -0.1 | -0.2 | -0.1 | -0.5 | -0.7 | -0.8 |
| Investment rule: Public sector net investment no more than 3 per cent on average | | | | | | | |
| March 2020 pre-measures forecast | 2.0 | 2.3 | 2.4 | 2.4 | 2.4 | 2.4 | 2.4 |
| March 2020 post-measures forecast | 2.0 | 2.2 | 2.6 | 2.9 | 3.0 | 3.0 | 3.0 |
| Welfare cap: Specified welfare spending in 2024-25 (£ billion) | | | | | | | |
| March 2020 pre-measures forecast | 119.5 | 121.7 | 125.7 | 128.1 | 131.5 | 135.5 | 138.8 |
| March 2020 post-measures forecast | 119.5 | 119.0 | 122.6 | 124.3 | 127.0 | 130.2 | 133.5 |
| Debt-interest-to-revenue ratio: Interest costs no more than 6 per cent of revenue | | | | | | | |
| March 2020 pre-measures forecast | 4.1 | 3.8 | 3.2 | 3.2 | 3.1 | 2.9 | 2.7 |
| March 2020 post-measures forecast | 4.1 | 3.8 | 3.3 | 3.5 | 3.3 | 3.1 | 2.9 |

[1] A negative value means the current budget is in surplus.

### The current balance rule

4.22 Our central forecast shows a current budget surplus in 2022-23 of £11.7 billion. On a pre-measures basis, the Chancellor had a margin of 0.8 per cent of GDP (£20.8 billion), but the combined effect of Budget measures and the new migration regime adds £9.0 billion to current borrowing in the target year.

### The maximum investment rule

4.23 Public sector net investment averages 2.9 per cent of GDP between 2020-21 and 2024-25, thereby meeting the new target with a margin of 0.1 per cent of GDP (£2.6 billion in today's terms). On a pre-measures basis, it averaged 2.4 per cent of GDP, with the Budget package raising that by a fifth. The increase is dominated by higher CDEL spending thanks to the much higher envelope set for the Spending Review.

4.24 Some of the larger contributors to PSNI are the capital transfers recorded alongside student loan outlays to recognise the amounts expected to be written off rather than repaid. These average 0.5 per cent of GDP between 2020-21 and 2024-25 and rise over time. The decision not to go ahead with further sales of student loans at a discount to their value in the public finances means our post-measures forecast for student loan capital transfers is 0.1 per cent of GDP lower on average over the period than it would otherwise have been.

### The debt interest to revenue ratio rule

4.25 Net interest payments are forecast to fall in cash terms over the next five years, so with receipts rising steadily the debt interest to revenue ratio falls from 3.8 per cent in 2019-20 to 2.9 per cent in 2024-25 – meeting the rule.

4.26 Budget measures and other Government decisions have raised the ratio in every year of the forecast and by an average of 0.2 percentage points. That difference reflects the 5.6 per cent average upward revision to net interest payments (on the back of higher effective interest rates, particularly Bank Rate, and higher cash borrowing) being greater than the 1.4 per cent upward revision to non-interest receipts (thanks to cancellation of the previously planned corporation tax cut that was due in April 2020, plus the boost to nominal GDP and the major tax bases associated with fiscal easing announced in the Budget).

### Table 4.6: Performance against the Budget 2020 fiscal and welfare targets

| | | Per cent of GDP | | £ billion | |
|---|---|---|---|---|---|
| | | Forecast | Margin | Forecast | Margin |
| Current budget rule: Current budget balanced by 2022-23[1] | | | | | |
| March 2020 pre-measures forecast | Met | -0.8 | 0.8 | -20.8 | 20.8 |
| March 2020 post-measures forecast | Met | -0.5 | 0.5 | -11.7 | 11.7 |
| Investment rule: Public sector net investment no more than 3 per cent on average | | | | | |
| March 2020 pre-measures forecast | Met | 2.4 | 0.6 | | |
| March 2020 pre-measures forecast | Met | 2.9 | 0.1 | | |
| Welfare cap: Specified welfare spending in 2024-25 (£ billion) | | | | | |
| March 2020 pre-measures forecast | Met | | | 138.8 | 4.1 |
| March 2020 post-measures forecast | Met | | | 133.5 | 4.1 |
| Debt-interest-to-revenue ratio: Interest costs no more than 6 per cent of revenue | | | | | |
| March 2020 pre-measures forecast | Met | 3.2 | 2.8 | | |
| March 2020 post-measures forecast | Met | 3.5 | 2.5 | | |

[1] A negative value means the current budget is in surplus.

## Recognising uncertainty

4.27 The future is uncertain and unexpected economic and political developments mean that the distribution of possible outcomes around any central forecast is wide. Consequently, there are significant upside and downside risks to our central public finance forecasts. These reflect uncertainty both about the outlook for the economy and about the level of receipts and spending in any given state of the economy.

4.28 Given these uncertainties, it is important to stress-test our assessment of the Government's performance against the proposed fiscal targets. We do this by:

- looking at the evidence of past forecast errors;
- seeing how our central forecast changes when we apply different individual judgements and assumptions; and
- looking at alternative scenarios.

## Past performance

4.29 One relatively easy way to assess the uncertainty around our central forecast is to look at the differences between previous official public finance forecasts – both our own and the Treasury's before us – and outturns. In doing so, we adjust for some changes in the definitions of these metrics (particularly when they led to systematic differences between current and contemporary estimates of outturn). The uncertainty can then be illustrated using fan charts like those in Chapter 2.

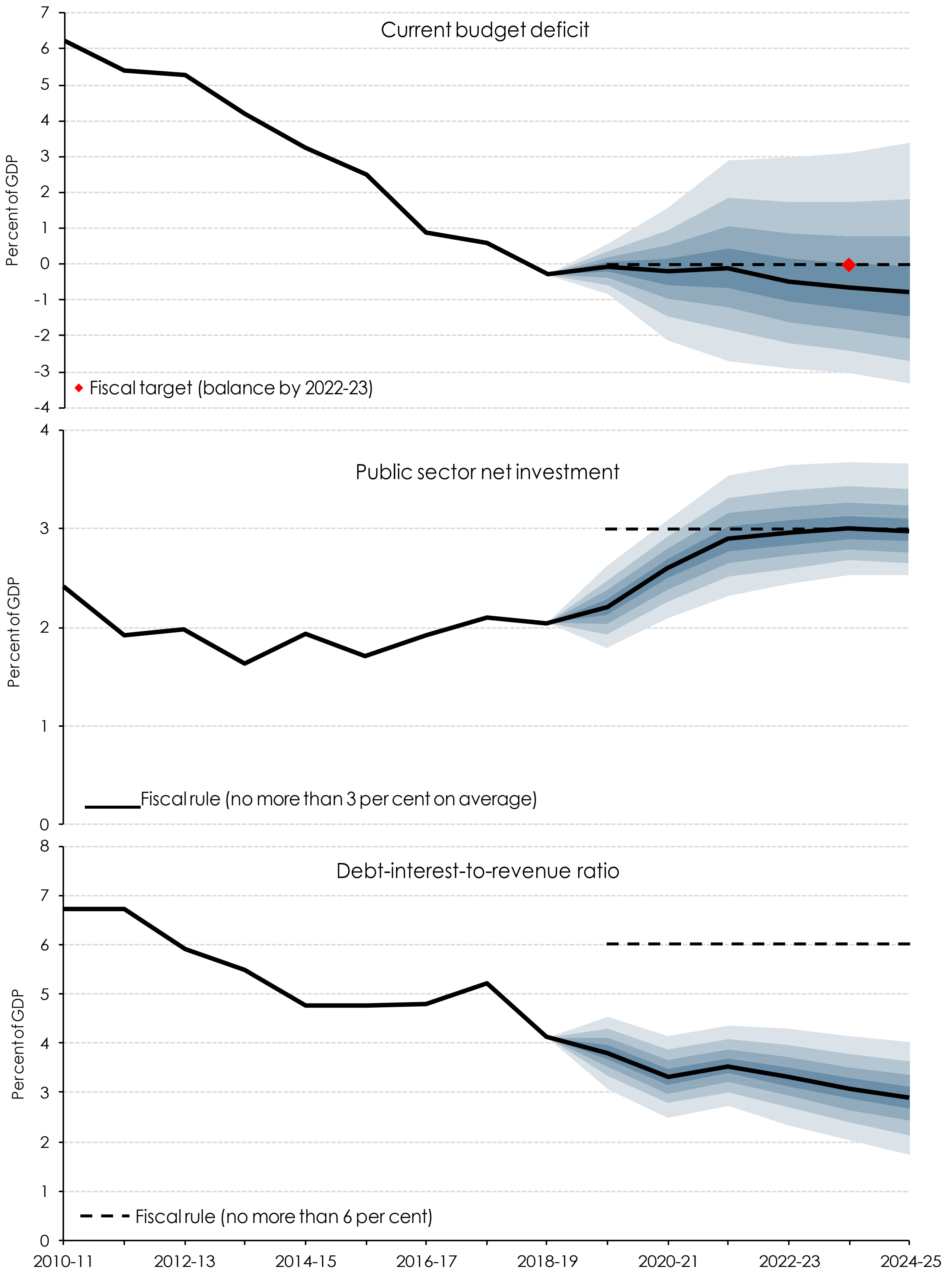
4.30 For the current budget deficit and PSNI, we have official forecasts going back to the late 1990s. But the Treasury did not publish forecasts for the debt-interest-to-revenue ratio, so we have only been able to construct historical forecasts for this from 2010 onwards. Outturn data can currently only be compared against the final forecast year for nine forecasts and, in each of these, the ratio was lower in outturn than we predicted (with an average five-year ahead forecast error of 2.6 percentage points). It is hard to see how this pattern of past forecast errors could be repeated with interest rates already close to zero. So we have simply assumed that past errors are representative of a symmetric future distribution.

4.31 The fan charts based on these forecasts do not represent a subjective assessment of specific risks to each forecast. Instead they show the outcomes someone might expect if they believed, rightly or wrongly, that the size and distribution of forecast errors in the past offered a reasonable guide to their future size and distribution.

4.32 It is important to note that the historical forecast errors that underpin our fan charts reflect both underlying forecast errors and subsequent policy responses. That helps explain why the probability distributions around borrowing and other measures of the budget balance do not widen significantly at longer horizons: when events or forecast changes push expected borrowing away from original plans, governments tend to implement policy changes to bring it back on track. This was evident in the analysis of past fiscal forecast errors and the fiscal policy response of governments presented in Annex B of our March 2016 *EFO*.

4.33 Chart 4.5 shows fans around our central forecasts for each of the Budget 2020 fiscal rules. Based on past forecast performance, the chance of the current budget being in surplus in the target year is around 60 per cent and it remains at around that level thereafter. The chance of net investment being less than 3 per cent of GDP falls from around 85 per cent in 2020-21 to around 50 per cent in 2024-25. Assuming that our forecasts will be as (in)accurate as they have been in the past, but that the risks are symmetric, the debt interest to revenue rule is almost certain to be met in every year. The Government therefore has much more room for manoeuvre relative to this rule than the other two.

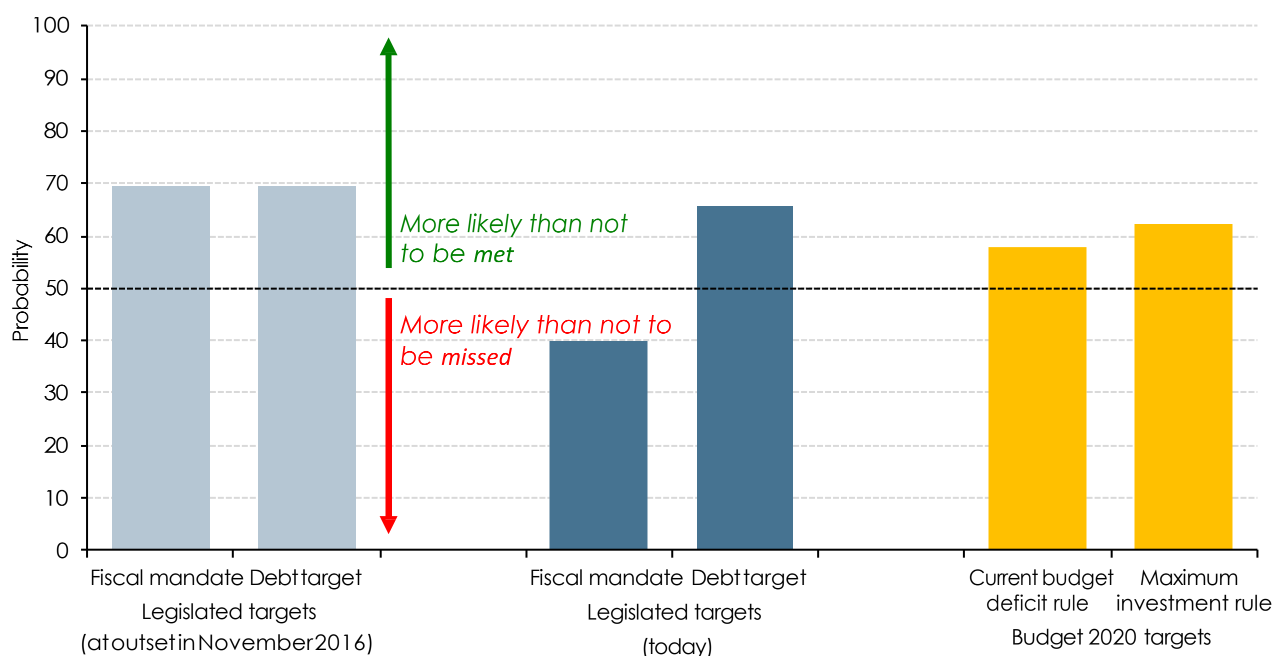
## Chart 4.5: Budget 2020 fiscal rule metrics: fan charts




Source: ONS, OBR

4.34 Chart 4.6 uses these fan charts to calculate the probability of each of the Budget 2020 fiscal rules being observed and compares it to the likelihood of the legislated targets being met, based both on our latest forecast and the margins by which they were met when they were introduced in November 2016. (All are based on the full historical distribution of forecast errors.) The chart demonstrates that when the current rules were introduced in November 2016, the Government gave itself more headroom against its new borrowing and debt targets than this Government has given itself against the Conservative manifesto targets.

## Chart 4.6: Likelihood of meeting the legislated and Budget 2020 fiscal rules




Source: OBR

## Sensitivity analysis

4.35 It is next to impossible to produce a full probability distribution for the Government's target fiscal variables because they are affected by so many determinants – both economic and non-economic – many of which are also interrelated in complex ways. But there are several particular sensitivities that are worth singling out:

- the sensitivity of the current budget deficit to changes in the level of GDP, inflation, interest rates and the effective tax rate;
- the sensitivity of public sector net investment to changes in departmental underspends, non-departmental spending, depreciation and nominal GDP;
- the sensitivity of the debt interest to revenue ratio to movements in factors affecting the numerator and the denominator in the ratio; and
- the sensitivity of the change in the debt-to-GDP ratio to factors that are not constrained by the other targets.

## The current budget deficit

4.36 As Chart 4.6 illustrated, on the basis of past forecast errors, we estimate that there is a roughly 40 per cent chance that the current budget will be in deficit in 2022-23. There are many reasons why this might happen. For example, the evolution of the economy could be less favourable than forecast (as is highly likely in the near term), or receipts or spending could turn out differently for a given state of the economy. And policy can also be expected to change at future Budgets.

4.37 On our website we publish ready-reckoners that show how elements of the public finances could be affected by changes in some key determinants. It is important to stress that these are stylised exercises that reflect the typical impact of changes in variables on receipts and spending as embodied in our forecast models. The actual impact in any given case is likely to depend on the state of the economy at the time and the reaction of other policymakers, notably the Monetary Policy Committee. The ready-reckoners are also subject to significant uncertainty. But with all this in mind, we can use them to calibrate several possible adverse surprises relative to our central forecast that would be sufficient to push the current budget into deficit in 2022-23.

4.38 The surplus of 0.5 per cent of GDP on the current budget could fall to zero if:

- The output gap were 0.7 per cent more negative or potential output 0.9 per cent lower. As the scenario below illustrates, the nature of any shock to potential output can affect these sensitivities, with a shock that feeds through to interest rates likely to have a smaller impact than one that does not. This change in potential output is small relative to the cumulative downward revisions made since the financial crisis.

- The effective tax rate (as measured by the tax-to-GDP ratio) were 0.5 percentage points lower. This could reflect structural or cyclical factors.

- Effective interest rates on central government gross debt were 0.6 percentage points higher. The £377 billion of conventional gilts held in the APF are currently in effect financed at Bank Rate, reducing the effective interest rate across all debt by 0.4 percentage points relative to gilt rates.

- RPI inflation were 2.3 percentage points higher than expected in 2022-23. Higher RPI inflation would increase accrued interest on index-linked gilts. Taken in isolation, this change alone would raise debt interest costs by 0.5 per cent of GDP. Higher oil prices or a substantial fall in the exchange rate could deliver such a surprise, as they did in the wake of the financial crisis. Of course, such shocks would have other effects on the public finances.

## The maximum investment rule

4.39 Average net investment over our forecast period is 2.9 per cent of GDP, giving the Government a 0.1 per cent of GDP margin against its maximum investment rule.

4.40 As this target is expressed as an average over five years, it is less sensitive to movements in public sector net investment in any individual year than a target focused on a particular year would be. That said, an increase in PSNI of only 0.1 per cent of GDP (£2.6 billion in today's terms) in *every* year would be sufficient to breach the rule. A single-year increase of 0.6 per cent of GDP (£12.8 billion in today's terms) would also be sufficiently large.

4.41 Most capital spending is subject to a degree of Treasury control rather than depending on exogenous economic factors. So this target is less sensitive to underlying forecast movements than the other two. The Treasury could change spending plans were our pre-measures forecast to overshoot the 3 per cent target.

4.42 Nonetheless, the margin against this target is much smaller than the other two, and numerous developments could see it used up:

- Persistently higher capital spending that averaged 0.1 per cent of GDP a year. As regards departmental spending, our central forecast assumes underspending relative to plans will average 0.3 per cent of GDP, so if actual underspending were 41 per cent lower the rule would be breached. Other public sector capital spending includes the capital transfers recorded when issuing student loans. We revised up our pre-measures forecast for these transfers by £2.0 billion a year on average in this forecast. Were that to be repeated, it would be sufficient to use up most of the margin against this rule.

- A temporary increase in spending due to a one-off transfer of 0.5 per cent of GDP. Capital grants to the private sector are classified as PSNI, and these, along with changes to their treatment in the public finances, can lead to large swings in this metric. Based on the accounting treatment underpinning our March 2012 forecast, the reclassification of the Royal Mail pension fund into the public sector reduced PSNI in 2012-13 by 1.8 per cent of GDP (£40 billion in today's terms). Classification changes later revised the impact on PSNI to a 0.6 per cent of GDP increase (£13 billion in today's terms). Another one-off increase of that size would be sufficient to erode the margin against this rule.

- The margin would fall to zero if the nominal GDP denominator were more than 3.8 per cent lower than our central forecast across the forecast period.

## The debt-interest-to-revenue ratio

4.43 We forecast the debt-interest-to-revenue ratio to peak at (3.5 per cent) in 2021-22 and to fall thereafter, leaving ample room to spare. Indeed, it would take very large surprises in individual variables to use up the margin in 2021-22, when it is at its smallest. Holding non-interest revenue constant, net interest spending would need to be £22 billion higher – on its own, Bank Rate hitting 6 per cent would do that. Holding net interest payments

constant, non-interest receipts would need to be £360 billion lower – a significantly larger fall than was seen in the financial crisis.

### The change in the debt-to-GDP ratio

4.44 Adhering to the Budget 2020 rules would not guarantee that debt falls relative to GDP. As well as borrowing, the path of debt depends on two other factors: the net cost of financial transactions (which are not covered by the rules) and the rate of nominal GDP growth (over which inflation-targeting governments have little control):

- Assuming our central forecast for financial transactions and nominal GDP growth in 2024-25, if borrowing were 3 per cent of GDP, the debt-to-GDP ratio would increase by 0.5 percentage points (rather than falling as in our central forecast).

- If borrowing in 2024-25 were 3 per cent of GDP and nominal GDP growth matched our central forecast, even if the net cost of financial transactions was 0.5 per cent of GDP less than we expect, debt would still rise relative to GDP in that year.

- For debt to fall relative to GDP, the growth rate of the cash value of debt must be less than the rate of growth of nominal GDP. Starting from our central PSND forecast of £1,969 billion in 2023-24, borrowing of 3 per cent of GDP plus financial transactions of 0.5 per cent of GDP would raise debt by 4.3 per cent in cash terms. That means nominal GDP growth would need to exceed our central forecast by 0.6 percentage points for the debt-to-GDP ratio to fall.

## Scenario analysis

4.45 The sensitivity analysis discussed above focuses on ready-reckoned estimates of the impact of individual factors and therefore offers only a limited assessment of potential uncertainty. In this section, we set out the fiscal implications of illustrative alternative scenarios, designed to test how dependent our conclusions are on key judgements. We stress that these scenarios are not intended to capture all possible ways in which the economy might deviate from the central forecast and we do not attempt to attach probabilities to them occurring.

4.46 We discuss the most pressing near-term source of forecast uncertainty – the economic implications of the spread of coronavirus – qualitatively in Box 2.3 in Chapter 2. It also quantifies the mechanical effects that movements in financial markets over the past three and a half weeks would have on our fiscal forecast. It is worth stressing, however, that whatever the short-term impact of coronavirus, the impact on the public finances over the medium and longer term is likely to be less significant, unless the outbreak inflicts lasting damage on the economy's supply capacity.

4.47 In this section we therefore explore the fiscal consequences of a key source of uncertainty over the longer term, namely the path of productivity. In particular, we examine the consequences of both weaker and stronger productivity growth than in our central forecast, calibrating the scenarios to converge on the pre- and post-crisis average growth rates. The

weak productivity scenario might crystallise if the global slowdown in productivity growth continues unabated or if the productivity hit from Brexit feeds through more quickly than we have assumed (a UK-specific event). The strong productivity scenario could occur if, by contrast, there were a general global pick-up in productivity growth.

4.48 To ensure that one scenario is not simply a mirror image of the other, we assume that the weak productivity scenario is a UK-specific event. The main consequence of this lies in the resulting path of interest rates, as one would expect a global change in productivity growth to be associated with a corresponding change in the global natural real rate of interest.

4.49 Specifically:

- The weak productivity scenario assumes that growth in potential output per hour averages 0.5 per cent a year over the next five years, in line with the post-crisis average. The level of productivity is therefore 3.1 per cent lower than in our central forecast by the first quarter of 2025. We assume that people increase the hours they work to offset in part the effect on their incomes. This leaves the level of real GDP 2.2 per cent below our central forecast. In expenditure terms, investment is reduced proportionately more than private consumption, reducing capital deepening. Lower productivity growth feeds through to weaker earnings growth, which averages 2.9 per cent a year. That also implies slower house price inflation, which averages 4.0 per cent a year. We assume the same path for interest rates as in our central forecast.

- The strong productivity scenario assumes that growth in potential output per hour picks up in the coming years and reaches 2.2 per cent in the final year of the scenario, in line with the pre-crisis average. The level of productivity is 3.1 per cent higher than our central forecast at the five-year horizon. We again assume that people adjust their hours, leaving real GDP 2.2 per cent higher than in our central forecast, and that investment is boosted proportionately more than consumption. Earnings growth averages 3.7 per cent a year and house price inflation 5.7 per cent a year. We assume higher interest rates than in our central scenario, consistent with the view that a revival of productivity growth globally would also raise the natural rate of interest.

4.50 In both scenarios, the output gap profile is unchanged, so that potential and actual growth are adjusted in equal measure. CPI inflation and unemployment are therefore also unchanged from our central forecast. RPI inflation is adjusted to reflect different paths for house prices and interest rates, which affect the housing depreciation and mortgage interest payments components of the RPI.

4.51 We have also considered a third scenario in which the Government delivers all the capital spending plans it has set out in the Budget, rather than assuming significant underspends relative to those plans as we do in our central forecast:

- This no underspend scenario adds between 0.1 and 0.2 per cent of GDP to CDEL spending across the forecast period, since our central forecast assumes that 20 per cent of the large increases in CDEL totals will go unspent. We have then used a

simplified version of the modelling in our central forecast to calculate the implications for GDP growth, interest rates and inflation. The scenario has relatively modest effects on economic outcomes. Higher government investment raises near-term GDP growth a little more than in our central forecast. But this induces a modestly higher path for Bank Rate, with GDP growth slowing slightly more than in our central forecast as a little more private sector expenditure is crowded out. We assume the supply side of the economy is unchanged within the forecast period, so the level of GDP at the end of the five-year period is the same as in our central forecast.

## Table 4.7: Key economic aggregates under alternative scenarios

| | Per cent on a year earlier, unless otherwise stated | | | | | |
|---|---|---|---|---|---|---|
| | Central forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| GDP growth | 1.1 | 1.3 | 1.7 | 1.4 | 1.3 | 1.5 |
| Output gap (per cent of potential GDP) | 0.0 | 0.1 | 0.4 | 0.4 | 0.1 | 0.0 |
| CPI inflation | 1.8 | 1.4 | 1.9 | 2.1 | 2.0 | 2.0 |
| Bank Rate (per cent) | 0.8 | 0.8 | 0.8 | 0.8 | 0.8 | 0.8 |
| Nominal GDP | 3.0 | 3.3 | 3.9 | 3.5 | 3.4 | 3.6 |
| | Weak productivity scenario | | | | | |
| GDP growth | 1.1 | 1.2 | 1.3 | 1.0 | 0.8 | 0.9 |
| Output gap (per cent of potential GDP) | 0.0 | 0.1 | 0.4 | 0.4 | 0.1 | 0.0 |
| CPI inflation | 1.8 | 1.4 | 1.9 | 2.1 | 2.0 | 2.0 |
| Bank Rate (per cent) | 0.8 | 0.8 | 0.8 | 0.8 | 0.8 | 0.8 |
| Nominal GDP | 3.0 | 3.2 | 3.5 | 3.1 | 2.8 | 3.0 |
| | Strong productivity scenario | | | | | |
| GDP growth | 1.1 | 1.4 | 1.9 | 1.9 | 1.9 | 2.1 |
| Output gap (per cent of potential GDP) | 0.0 | 0.1 | 0.4 | 0.4 | 0.1 | 0.0 |
| CPI inflation | 1.8 | 1.4 | 1.9 | 2.1 | 2.0 | 2.0 |
| Bank Rate (per cent) | 0.8 | 0.8 | 1.0 | 1.3 | 1.4 | 1.3 |
| Nominal GDP | 3.0 | 3.4 | 4.1 | 4.0 | 4.0 | 4.2 |
| | No underspend scenario | | | | | |
| GDP growth | 1.1 | 1.4 | 1.7 | 1.4 | 1.2 | 1.4 |
| Output gap (per cent of potential GDP) | 0.0 | 0.1 | 0.5 | 0.4 | 0.2 | 0.0 |
| CPI inflation | 1.8 | 1.4 | 2.0 | 2.1 | 2.1 | 2.0 |
| Bank Rate (per cent) | 0.8 | 0.8 | 0.8 | 0.8 | 0.8 | 0.8 |
| Nominal GDP | 3.0 | 3.4 | 3.9 | 3.5 | 3.3 | 3.6 |

### Fiscal implications

4.52 Based on these assumptions, Table 4.8 sets out each scenario's main fiscal effects:

- In the weak productivity scenario, lower growth in average earnings, profits, house prices and equity prices lower receipts and increase borrowing and debt. Spending increases initially, as a greater proportion of student loan outlays is written off at outlay. But it is lower from 2022-23 onwards, as lower RPI inflation reduces debt interest and weaker earnings growth lowers the cost of the state pensions triple lock.

- In the strong productivity scenario, the boost to receipts from stronger growth in all the major tax bases more than offsets higher spending. The increase in state pension spending due to the triple lock eventually outweighs the lower spending on student loans from writing off a smaller proportion of loans on outlay. The fiscal implications of this scenario are not quite the weak productivity scenario in reverse: interest rates are higher, so debt interest rises by £6.8 billion in 2024-25, partly offsetting the saving associated with lower primary borrowing.

- The main effect in the no underspend scenario is, of course, higher capital spending – by just under £4 billion a year on average from 2021-22 onwards. There are relatively small effects on the rest of our forecast. Higher spending boosts the economy in the near term, which raises tax receipts and lowers borrowing, but this effect dissipates by the end of the period. Higher borrowing and higher interest rates increase debt interest spending in all years, while higher capital spending also raises depreciation costs modestly. By 2024-25, these indirect effects raise borrowing by around £0.4 billion.

## Performance against the fiscal targets

4.53 The Government is not on course to meet its legislated fiscal mandate in our central forecast, nor in any of the scenarios either. The legislated fiscal objective looks even more unlikely to be met in the weak productivity and no underspend scenarios. Indeed, borrowing is still around 2 per cent of GDP in 2024-25 in the high productivity scenario. The Government still meets the legislated supplementary target for debt to fall in 2020-21 in all scenarios, as TFS loans are repaid.

4.54 What about the Budget 2020 fiscal targets? As Table 4.8 shows, the current budget rule is met in all scenarios, though the margin drops to just 0.2 per cent of GDP in the weak productivity scenario. The maximum investment rule is met in both productivity scenarios, although in the weak one PSNI tops 3 per cent of GDP from 2022-23 onwards, so it is only met thanks to investment being well below 3 per cent in 2020-21. The rule is missed in the no underspend scenario, so the Government's plans are in a sense inconsistent with its rule. The debt-interest-to-revenue ratio remains comfortably below 6 per cent in all years of all three scenarios.

## Table 4.8: Key fiscal aggregates under alternative scenarios

| | Per cent of GDP, unless otherwise stated | | | | | |
|---|---|---|---|---|---|---|
| | Central forecast | | | | | |
| | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Legislated objective and targets | | | | | | |
| Public sector net borrowing | 2.1 | 2.4 | 2.8 | 2.5 | 2.4 | 2.2 |
| Cyclically adjusted net borrowing | 2.2 | 2.4 | 3.0 | 2.7 | 2.5 | 2.2 |
| Public sector net debt | 79.5 | 77.4 | 75.0 | 75.4 | 75.6 | 75.2 |
| Budget 2020 fiscal targets | | | | | | |
| Current budget deficit | -0.1 | -0.2 | -0.1 | -0.5 | -0.7 | -0.8 |
| Public sector net investment | 2.2 | 2.6 | 2.9 | 3.0 | 3.0 | 3.0 |
| Debt-interest-to-revenue ratio | 3.8 | 3.3 | 3.5 | 3.3 | 3.1 | 2.9 |
| | Weak productivity scenario | | | | | |
| Legislated objective and targets | | | | | | |
| Public sector net borrowing | 2.2 | 2.5 | 3.0 | 2.8 | 2.9 | 2.9 |
| Cyclically adjusted net borrowing | 2.2 | 2.5 | 3.2 | 3.1 | 3.0 | 2.9 |
| Public sector net debt | 79.5 | 77.6 | 75.6 | 76.6 | 77.6 | 78.3 |
| Budget 2020 fiscal targets | | | | | | |
| Current budget deficit | -0.1 | -0.2 | 0.0 | -0.2 | -0.2 | -0.2 |
| Public sector net investment | 2.2 | 2.6 | 3.0 | 3.0 | 3.1 | 3.1 |
| Debt-interest-to-revenue ratio | 3.8 | 3.3 | 3.5 | 3.3 | 3.1 | 2.9 |
| | Strong productivity scenario | | | | | |
| Legislated objective and targets | | | | | | |
| Public sector net borrowing | 2.1 | 2.4 | 2.7 | 2.3 | 2.0 | 1.7 |
| Cyclically adjusted net borrowing | 2.1 | 2.4 | 3.0 | 2.6 | 2.1 | 1.7 |
| Public sector net debt | 79.5 | 77.4 | 74.8 | 74.8 | 74.2 | 73.0 |
| Budget 2020 fiscal targets | | | | | | |
| Current budget deficit | -0.1 | -0.2 | -0.1 | -0.6 | -0.9 | -1.2 |
| Public sector net investment | 2.2 | 2.6 | 2.9 | 2.9 | 2.9 | 2.9 |
| Debt-interest-to-revenue ratio | 3.8 | 3.4 | 3.8 | 3.8 | 3.5 | 3.4 |
| | No underspend scenario | | | | | |
| Legislated objective and targets | | | | | | |
| Public sector net borrowing | 2.1 | 2.4 | 2.9 | 2.6 | 2.5 | 2.4 |
| Cyclically adjusted net borrowing | 2.2 | 2.5 | 3.2 | 2.9 | 2.7 | 2.4 |
| Public sector net debt | 79.5 | 77.4 | 75.1 | 75.7 | 76.0 | 75.8 |
| Budget 2020 fiscal targets | | | | | | |
| Current budget deficit | -0.1 | -0.2 | -0.1 | -0.5 | -0.7 | -0.8 |
| Public sector net investment | 2.2 | 2.7 | 3.0 | 3.1 | 3.1 | 3.1 |
| Debt-interest-to-revenue ratio | 3.8 | 3.3 | 3.6 | 3.4 | 3.1 | 2.9 |

# Executive summary

## Overview

1 In our *Fiscal sustainability report* (*FSR*) we look beyond the medium-term forecast horizon of our twice-yearly *Economic and fiscal outlooks* (*EFOs*) and ask whether the UK's public finances are likely to be sustainable over the longer term.

2 In doing so our approach is twofold:

- first, we look at the fiscal impact of *past* government activity, as reflected in the assets and liabilities on the public sector's balance sheet; and
- second, we look at the potential fiscal impact of *future* government activity, by making 50-year projections of all public spending, revenues and significant financial transactions, such as government loans to students.

3 Our projections are based on current stated Government policy, but in three key instances policy formation is ongoing:

- Our projections include the impact of the Government's as-yet unfunded June 2018 announcement of increased health spending over the medium term. The Government has indicated that measures to finance at least part of the additional spending will be announced at some point, but has given no firm details of their size or composition.
- Following the Government's December 2017 decision not to implement the Dilnot reforms to adult social care funding it planned for 2020, we have removed them from our projections, reducing projected spending. The Government says it will announce new policy proposals in due course, which could push projected spending up again.
- The Government's July 2017 State Pension age (SPA) review gave greater clarity on the probable timing of future increases to the SPA and we have included the consequences of this. The Government has also said that it will review the continued operation of triple-lock uprating of the state pension beyond this Parliament, potentially reducing projected spending. But in the absence of a firm decision to replace the triple lock we assume that it remains in place.

4 With or without these policy changes, our projections suggest that the public finances are likely to come under significant pressure over the longer term, due to an ageing population and further upward pressure on health spending from factors such as technological advances and the rising prevalence of chronic health conditions. Under our definition of unchanged policy, the Government would end up having to spend more as a share of

national income on age-related items such as pensions and (in particular) health care, but the same demographic trends would leave government revenues roughly stable.

5 In the absence of offsetting tax rises or spending cuts, this would widen the government's budget deficit over time and put public sector net debt on an unsustainable upward trajectory. This fiscal challenge from an ageing population and from additional pressures on health spending is common to many developed nations.

6 The long-term outlook for the public finances is less favourable than at the time of our last *FSR* in January 2017. This is more than explained by the June health spending announcement, which – in the absence of accompanying offsetting tax or spending measures – increases spending by significantly more than the modest fiscal tightening implied by dropping the Dilnot reforms and accelerating rises in the State Pension age. If the higher health spending were to be fully financed by tax rises or cuts in other spending, the long-term outlook for the public finances would be little changed from our 2017 *FSR*. The latest population projections from the ONS weaken the long-term fiscal position, with prospective demographic trends slightly less favourable to the public finances.

7 Long-term projections such as these are highly uncertain and the results we present here should be seen as illustrative scenarios conditioned on particular 'what if' assumptions, not as precise forecasts. We quantify some of the uncertainties through sensitivity analyses, particularly relating to demography and health spending.

8 It is important to emphasise that we focus here on the additional fiscal tightening that might be necessary to achieve fiscal sustainability beyond our medium-term forecast horizon, which currently ends in 2022-23. Our March 2018 forecast incorporated the modest further fiscal tightening then planned by the Government over the medium term – primarily further cuts to departmental current spending as a share of GDP and cuts to working-age welfare spending. In the absence of offsetting tax or spending policies that have yet to be specified, the subsequent June health spending announcement leaves the deficit broadly flat over the medium term in the figures we use in this report, rather than narrowing.

9 While it is not for us to recommend the size or timing of any additional fiscal tightening measures, policymakers and would-be policymakers should certainly think carefully about the long-term consequences of any policies they introduce or propose in the short term, including at next year's Spending Review. And they should give thought too to the policy choices that will confront them once the current planned consolidation is complete.

## Public sector balance sheets

10 We assess the fiscal impact of past government activity by looking at the assets and liabilities on the public sector's balance sheet. We look at two presentations of the balance sheet: the National Accounts and the 2016-17 Whole of Government Accounts (WGA).

11 The last three governments have set targets for the National Accounts measure of public sector net debt (PSND) – the difference between the public sector's debt liabilities and liquid

financial assets. At the end of 2017-18, PSND stood at £1,779 billion, equivalent to 85.4 per cent of GDP or £65,000 per household. Thanks in part to significant planned asset sales during 2018-19, our March forecast assumed that PSND would peak as a share of GDP in 2017-18. The medium-term debt profile in this report is little changed from that in our 2017 *FSR*, with the impact of the June health spending increase offset by the reclassification of English housing associations and their borrowing and debt to the private sector in November 2017. However, the latter does not fundamentally improve the health of the public finances.

12 National Accounts balance sheet measures do not include liabilities arising from the future consequences of past government activities, for example the pension rights that have been accrued by public sector workers. More information on liabilities of this sort is available in the WGA, which are produced using commercial accounting rules.

13 According to the 2016-17 WGA, as of the end of March 2017:

- The net present value of future public service pension payments arising from past employment was £1,835 billion or 92 per cent of GDP. This is £410 billion higher than a year earlier, with the rise more than explained by the use of a lower discount rate to convert the projected flow of future payments into a one-off net present value and by other changes to assumptions underpinning the value of the liabilities. (Unfortunately, the WGA do not split these out transparently.)

- The public sector's liabilities include £322 billion (16 per cent of GDP) in provisions for future costs that are expected (but not certain) to arise. They have increased by £17 billion since 2016-17. The three largest sources of provisions – for future nuclear decommissioning costs (particularly at Sellafield), for clinical negligence claims and for the Pension Protection Fund – all increased significantly, by £3.2 billion, £9.0 billion and £3.2 billion respectively. Repeated and often large increases in provisions suggest that these could become significant future pressures on public spending.

- £84 billion (4 per cent of GDP) of quantifiable contingent liabilities had been identified. These are costs that could arise in the future, but where the probability of each of them in isolation doing so is estimated at less than 50 per cent (so they are not included in the headline total of liabilities). The £20 billion reduction compared with last year was more than explained by a £30.4 billion fall in HMRC's contingent liability associated with tax litigation cases, reflecting the cessation of litigation in some cases and revised cost estimates for some ongoing cases. This reduction was partially offset by a £9.8 billion increase relating to clinical negligence (for which the WGA record both provisions and contingent liabilities), due to the use of a lower discount rate to calculate compensation claims.

14 Overall, gross liabilities in the WGA increased by £595 billion over the year to reach £4,324 billion at the end of March 2017. In part this was explained by the net deficit of £98 billion recorded during the year, as expenditure exceeded revenue, but the majority reflected the use of a lower discount rate to estimate public service pension liabilities.

15 Unlike PSND, the WGA balance sheet also includes the value of tangible and intangible fixed assets – for example the road network and the electromagnetic spectrum respectively. These are estimated at £1,181 billion or 59 per cent of GDP at the end of March 2017. They have increased by £51 billion since last year's WGA, thanks to revaluation effects and new assets under construction. Total gross assets reached £1,903 billion, up £161 billion on last year.

16 The overall net liability in the WGA was £2,421 billion or 122 per cent of GDP at the end of March 2017, up £435 billion on the previous year's restated results. This compares with a £124 billion rise in PSND to £1,727 billion. The sharper rise in the WGA liability largely reflects the discount rate effect on the public service pensions liability.

17 There are significant limits to what public sector balance sheets alone can tell us about fiscal sustainability. In particular, balance sheet measures look only at the impact of past government activity. They do not include the present value of future spending that we know future governments will wish to undertake, for example on health, education and state pensions. Just as importantly, they exclude the public sector's most valuable financial asset – its ability to levy future taxes. So we should not overstate the significance of the fact that PSND and the WGA balance sheet both show the public sector's liabilities outstripping its assets. Across countries and time, this has usually been the case.

## Long-term fiscal projections

18 We assess the potential fiscal impact of future government activity by making long-term projections of revenue, spending and financial transactions on an assumption of 'unchanged policy', as best we can define it. In doing so, we usually assume that spending and revenues initially evolve over the next five years as we forecast in our most recent *EFO*. We have departed from this approach in this *FSR* by incorporating the significant increase in NHS spending through to 2023-24 announced by the Prime Minister in June (and including an assumption about its 'Barnett consequentials' for health spending outside England).

19 We incorporate this announcement both because it is very large compared to most policy announcements outside scheduled fiscal events and because health is the most important component in our long-term analysis. The Government has indicated that it will fund at least some of the health package by increasing taxes and/or reducing other spending, but in the absence of firm detail we cannot include this in our projections. It has also said that the announcement will be funded in part by a 'Brexit dividend', although our provisional analysis suggests Brexit is more likely to weaken than strengthen the public finances overall. There will be direct savings from the net contributions to the EU budget that the UK will no longer have to make, but it is unclear how much will be available after payments towards the agreed withdrawal settlement and other Brexit-related spending commitments.

20 We have not made any further judgements or assumptions about the nature of the UK's departure from the European Union beyond those that underpinned our March *EFO*.

## Demographic, economic and health-specific assumptions

21 Demographic change is a key long-term pressure on the public finances. Like many developed nations, the UK is projected to have an ageing population over the next few decades, with the old-age dependency ratio – the ratio of the elderly to those of working age – rising. This reflects increasing life expectancy (particularly among older people), relatively low fertility rates, and the retirement of the post-war 'baby boom' cohorts.

22 We base our analysis on detailed population projections produced by the Office for National Statistics (ONS). In this *FSR*, we use its 2016-based population projections, which were released in October 2017. As in our 2017 *FSR*, our baseline fiscal projections use the 'principal' ONS population projection. This assumes that net inward migration falls to 165,000 a year by 2022-23 and remains at that level thereafter. We test the sensitivity of our conclusions to using different ONS variants. Relative to the 2014-based projections that underpinned our 2017 *FSR*, lower net inward migration and fewer births reduce the working age population. As a result, the old-age dependency ratio now rises more rapidly than in our previous report, despite slower improvements in future life expectancy leading the ONS to revise down the projected number of elderly people by increasing amounts.

23 As regards the economy, we continue to assume in our baseline projection that whole economy productivity growth will average 2.0 per cent a year in steady state. We have made several small changes to the long-term economic determinants we use, including revising down GDP deflator inflation by 0.1 percentage points to 2.2 per cent a year and revising down employment growth due to slower growth in the adult population. Having revised down our medium-term productivity growth forecast significantly since our previous *FSR*, we now assume it takes longer for productivity growth to return to its steady state rate.

24 In this year's report, we continue to assume that health spending rises to accommodate non-demographic cost pressures beyond the medium term and that this adds 1 percentage point a year to health spending growth in the long term. We assume that excess cost growth falls from the latest available estimates for primary and secondary care (which are higher than 1 percentage point) back to this long-term assumption steadily over the period to 2038-39. This approach and the values that we have chosen are similar to those used by the US Congressional Budget Office. It is important to emphasise that our health spending projections are not based on any bottom-up assessment of 'need', but rather embody a judgement that 'unchanged policy' is best interpreted as assuming that spending rises to accommodate demographic and non-demographic cost pressures over time.

## Defining 'unchanged' policy

25 Fiscal sustainability analysis is designed to identify whether and when changes in government policy may be necessary to move the public finances from an unsustainable to a sustainable path. To make this judgement, we must first define what we mean by 'unchanged' policy over the long term for all tax and spending streams, not just health.

26 Government policy is rarely clearly defined over the long term. In many cases, simply assuming that a stated medium-term policy continues for 50 years would be unrealistic. Where policy is not clearly defined over the long term, the *Charter for Budget Responsibility* allows us to make appropriate assumptions. These are set out clearly in the report. Consistent with the *Charter*, we only include the impact of policy announcements in our baseline projections when they can be quantified with "*reasonable accuracy*".

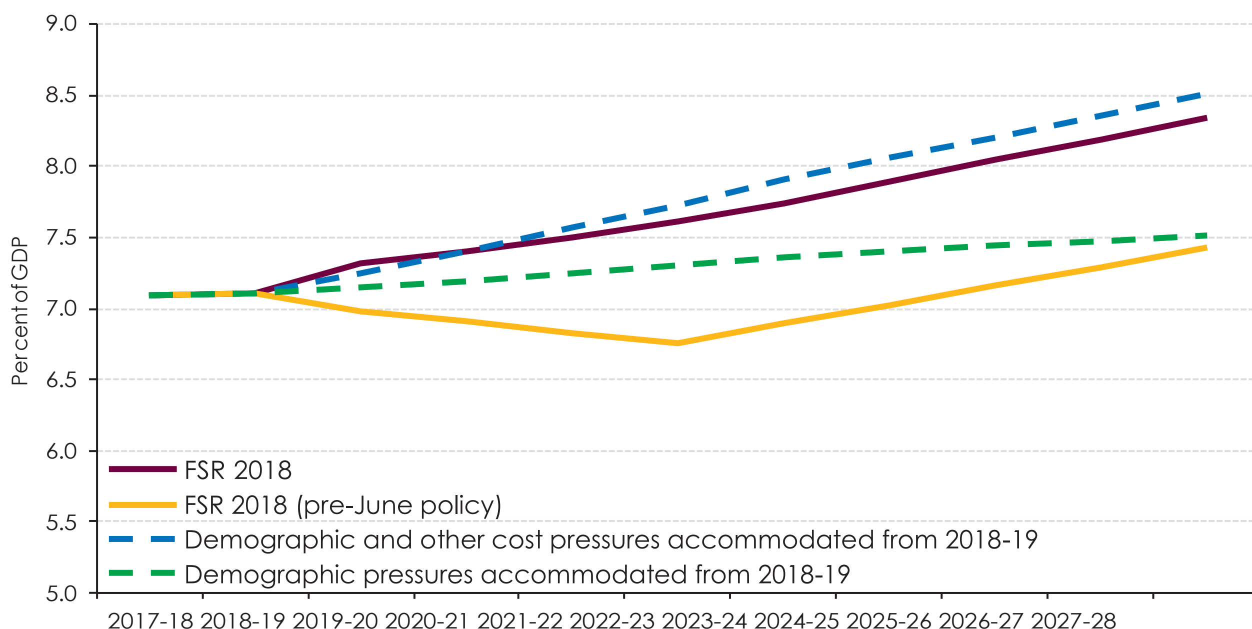
## Medium-term policy changes

27 Changes in the starting point for our projections are often an important driver of changes in the long-term projections from one *FSR* to the next. The net effect of the three *EFO* forecasts since our 2017 *FSR* has been relatively minor, but the June announcement of significantly higher health spending over the medium term has had a significant effect on our projections.

28 For the largest component of UK-wide health spending – the budget of NHS England – the Government has now set out current spending plans up to 2023-24, so our long-term assumptions start from 2024-25. The June announcement implies a real terms increase in spending of £20.5 billion by 2023-24, relative to an adjusted 2018-19 baseline. In 2022-23, the resulting increase in UK-wide health spending is 0.9 per cent of GDP (£20.5 billion in *cash* terms), relative to what we assume it would have been absent the announcement. (This includes an additional £1.25 billion to cover a "*specific pensions pressure*").

29 Chart 1 shows our baseline projection for UK-wide health spending over the next 10 years with and without the June announcement. The pre-announcement path declines steadily as a share of GDP to 2022-23, based on Government plans as they stood at the March 2018 Spring Statement, at which point our long-term assumptions would have put it back on an upward trend as a share of GDP. With the June announcement, health spending is on a rising path up to 2022-23 too, reaching 7.6 per cent of GDP (£181.8 billion).

### Chart 1: Impact of June 2018 NHS spending announcement




Source: HMT, OBR

30 Health spending is currently estimated at 7.1 per cent of GDP (£150.2 billion) in 2018-19, on the functional definition we use. If spending were to rise from that level to accommodate only demographic pressures, we estimate that it would reach 7.3 per cent of GDP (£174.4 billion) in 2022-23. If it rose sufficiently to accommodate other cost pressures as well, it would reach 7.7 per cent of GDP (£184.7 billion).

31 Absent the June 2018 announcement, we would have projected health spending at 6.8 per cent of GDP (£161.3 billion) in 2022-23, implying shortfalls against those two hypothetical paths of 0.5 per cent of GDP (£13.0 billion) and 1.0 per cent of GDP (£23.3 billion) respectively. The June 2018 announcement means that health spending is now projected to rise more than enough to meet the demographic cost pressures over those four years and sufficiently to meet around four fifths of the demographic and non-demographic pressures combined, leaving a shortfall of 0.1 per cent of GDP (£2.8 billion) against that counterfactual in 2022-23.

32 Given the significant uncertainty around estimates of these pressures, particularly the non-demographic ones, these paths and the gaps relative to them should be treated as illustrative. They do not represent a bottom-up assessment of the necessary level of health spending as a share of GDP, which would anyway lie beyond our remit.

33 Announcing the additional health spending, the Prime Minister said that it would be funded by a "*Brexit dividend, with us as a country contributing a little more*". As already noted, the Government has not set out the size or composition of any additional taxpayer contribution, either through higher taxes or cuts in other spending, so we have not been able to include it in our projections. As regards the 'Brexit dividend', our provisional analysis suggests that Brexit is more likely to weaken the public finances than strengthen them over the medium term, thanks to its likely effect on the economy and tax revenues. Looking more narrowly at direct financial flows with the EU, we estimated in our March 2018 *EFO* that the UK would have had to make a contribution of £13.3 billion to the EU budget in 2022-23 if we remained a member. Of that potential saving, £7.5 billion will be absorbed by the withdrawal settlement payment expected for that year, leaving £5.8 billion to be spent on other things. In principle this could cover slightly less than 30 per cent of the cost of health package in that year, but this does not take into account other calls on these potential savings, including commitments the Government has already made on farm support, structural funds, science and access to regulatory bodies. Pending a detailed withdrawal agreement and associated spending decisions, we assume in this report that the extra health spending adds to total spending and borrowing rather than being absorbed in whole or part elsewhere.

## Long-term policy assumptions

34 With the notable exception of non-demographic cost pressures in health, our baseline projection assumes that underlying age-specific spending on public services rises with per capita GDP beyond 2022-23.

35 We assume that most tax thresholds and benefits are uprated in line with earnings growth rather than inflation beyond the medium term, which provides a more plausible and fiscally neutral baseline for long-term projections. An inflation-based assumption would, other things equal, imply an ever-rising ratio of tax to national income and an ever-falling ratio of benefit payments to average earnings in the rest of the economy. In the past, policy has indeed tended to evolve to offset fiscal drag in the tax system.

36 We have assumed in our baseline projection that the 'triple lock' on state pensions uprating continues to apply – and that on average it leads to the state pension being uprated by 0.36 percentage points on top of earnings growth. The Chancellor has said that the Government will review whether this commitment will continue into the next Parliament "*in light of the evolving fiscal position at the next Spending Review*" – this is expected to be in 2019. We test the sensitivity of our projections to assuming earnings uprating instead of the triple lock, as this would be a plausible alternative interpretation of unchanged policy.

## Results of our projections

37 Having defined unchanged policy, we apply our demographic and economic assumptions to produce projections of the public finances over the next 50 years.

### Expenditure

38 An ageing population and health-specific cost pressures put upward pressure on public spending in our baseline projection. Total non-interest spending rises from 36.4 per cent of GDP at the end of our medium-term forecast in 2022-23 to 44.6 per cent by 2067-68. This increase of 8.2 per cent of GDP is equivalent to £172.8 billion a year in today's terms.

39 The main drivers are upward pressures on age-related spending:

- Health spending rises from 7.6 per cent of GDP in 2022-23 to 13.8 per cent in 2067-68 as the population ages and non-demographic cost pressures mount. The starting point for UK-wide health spending in 2022-23 is 0.6 per cent of GDP higher than it was in *FSR* 2017, more than explained by the 0.9 per cent of GDP effect of the NHS announcement in that year and its knock-on effects outside England, which is partly offset by our attributing more of the Better Care Fund to social care. Applying our long-term assumptions about demographic and other cost pressures, the first of which are a little more unfavourable than in our previous report, by 2067-68 the upward revision relative to *FSR* 2017 rises to 1.0 per cent of GDP.

- State pension costs increase from 5.0 per cent of GDP in 2022-23 to 6.9 per cent in 2067-68 as the population ages and the triple lock raises average awards relative to whole economy earnings. This profile is a little lower than in *FSR* 2017, mostly reflecting Government decisions that accelerate the pace of SPA increases.

- Adult social care costs rise from 1.3 per cent of GDP in 2022-23 to 1.9 per cent in 2067-68, reflecting the ageing of the population. The projections are slightly lower

than in our previous report as we have removed the effect of the Dilnot reforms that were included in our previous report. This is only partly offset by increasing the proportion of the Better Care Fund that we attribute to adult social care.

## Revenue

40 Demographic factors are expected to have much less impact on revenues than on spending. Non-interest revenues are projected to be all but flat as a share of GDP across the projection period. In our baseline projection, those revenue streams that are not affected by demographics are explicitly held constant as a share of GDP. As we have explored in previous reports, there are various non-demographic factors that may affect different revenue streams in the future, but these are not incorporated into our baseline projections.

## Financial transactions

41 To move from spending and revenue projections to an assessment of the outlook for public sector net debt, we also need to take public sector financial transactions into account. These affect net debt directly, without affecting accrued spending or borrowing.

42 For the majority of financial transactions, we assume that their net effect over the long term is zero. Student loans are an important exception. Lending to students adds to net debt immediately through financing the outlays. Repayments then reduce that addition, but not completely because some of the lending is expected to be written-off rather than repaid.

43 We have revised up our projection for the effect of student loans on net debt relative to our previous report. This largely reflects policy changes announced since then. In particular, the Government has raised the threshold at which students start repaying their loans from £21,000 in 2017-18 to £25,000 in 2018-19 and it plans to uprate this with average earnings over time. This significantly reduces the repayments made by students over the lifetime of their loans and consequently increases the write-offs at the end of the 30-year loan period. At the peak, student loans are now projected to increase net debt by 12.4 per cent of GDP in the late-2030s, before falling back slightly to 11.2 per cent of GDP in 2067-68. This latter figure is 1.9 per cent of GDP higher than our previous projection last year.

44 Alongside this *FSR* we publish a working paper on the accounting treatment of student loans and the fiscal illusions that this produces.[1] This is particularly true in respect of public sector net borrowing, which is flattered in the near term by interest receipts that are accrued in full but only expected to be paid in part, and which only recognises the cost of subsidising the loans far in the future when outstanding balances are written off after 30 years.

45 The Government continues to reduce the assets held by UK Asset Resolution (UKAR) through active sales and the natural rundown of mortgages and plans to sell much of its stake in RBS. The sale of financial assets is classified as a financial transaction in the public finances statistics. Sales reduce public sector net debt directly and indirectly (via net borrowing, because interest is paid on a smaller stock of debt), but typically (and in the case of these

[1] Ebdon and Waite, *Working Paper No. 12: Student loans and fiscal illusions*, OBR, July 2017.

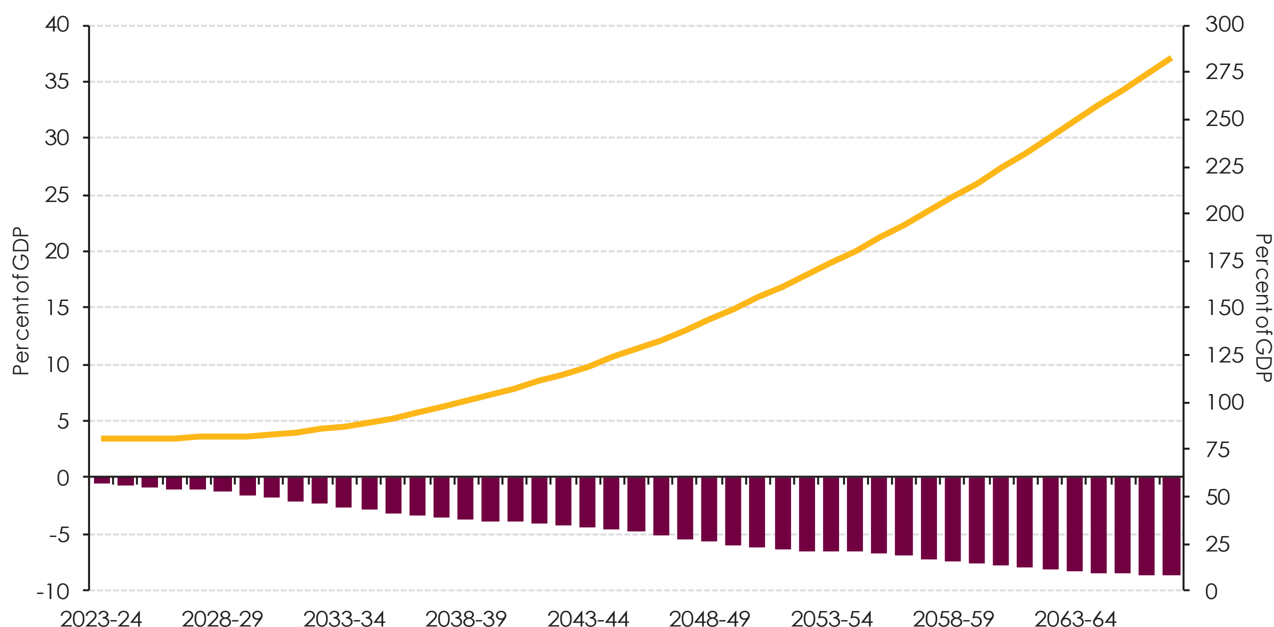
sales) the government also loses a related income stream. Over the long term, therefore, the net impact of asset sales on net debt is significantly less than the sale price. The effect on broader balance sheet measures is typically close to zero because the sales involve converting one asset (mortgages or shares) into another (cash).

## Projections of the primary balance and public sector net debt

46 Our baseline projections show public spending increasing as a share of national income beyond the medium-term forecast horizon, exceeding receipts by increasing amounts over the projection period. As a result, the primary budget deficit (the difference between non-interest revenues and spending) is projected to move from 0.3 per cent of GDP in 2022-23 to 8.6 per cent of GDP in 2067-68 – an eventual overall deterioration of 8.3 per cent of GDP, equivalent to £176.5 billion a year in that year in today's terms.

47 Taking this and our projection of financial transactions into account, PSND is projected to fall from its medium-term peak of 85.6 per cent of GDP in 2017-18 to 80.0 per cent of GDP in 2022-23, before rising thereafter and reaching 282.8 per cent of GDP in 2067-68. Beyond this point, debt would remain on a rising path. Needless to say, in practice policy would need to change long before this date to prevent this outcome.

### Chart 2: Baseline projections of the primary balance and PSND




Source: OBR

48 The primary deficit and PSND at the end of the projection period are considerably higher than in our 2017 *FSR* projections. As Table 1 shows, this reflects:

- Methodology changes to the calculation of debt interest. These do not affect the primary balance, but increase debt.

- Classification changes. English housing associations have been reclassified to the private sector, which has a small effect on the primary balance but a larger effect on net debt in the short term that increases over the projection period.

- More unfavourable demographics put upward pressure on age-related spending.

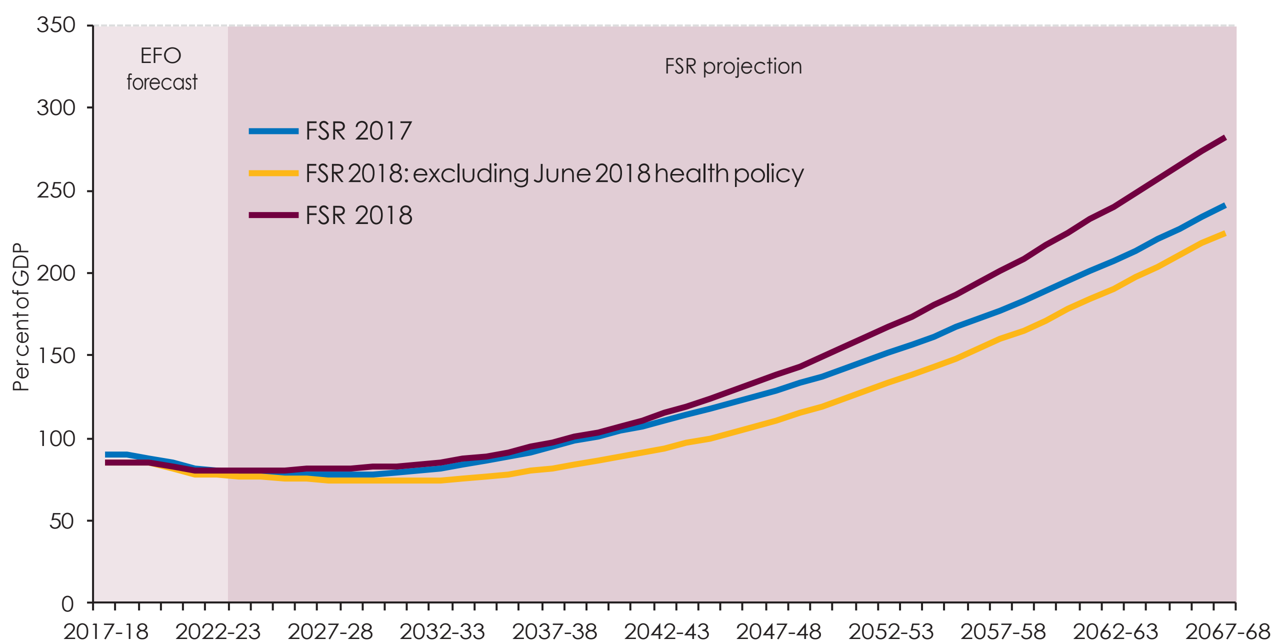
- Changes to long-term policy (including dropping the Dilnot reforms to adult social care and accelerating increases in the SPA) amount to a significant fiscal tightening over the long run, reducing the primary deficit by 0.4 per cent of GDP and net debt by 31.0 per cent of GDP in 2067-68. But we do not yet know what will replace the Dilnot reforms, so future policy changes could see spending and debt revised up again.

- The June 2018 health spending announcement increases the primary deficit and net debt at the start of our baseline projection and by increasing amounts thereafter. The effect in 2022-23 reflects the fact that the Government has specified the spending announcement in sufficient detail for us to include it in these projections, but has not provided any detail on how it will be financed (although it has indicated that tax rises are expected to finance at least some of it). The longer-term effect also includes the result of assuming that spending will continue to rise from that base to accommodate continuing demographic and other cost pressures. Overall it increases the primary deficit by 1.5 per cent of GDP and net debt by 57.9 per cent of GDP in 2067-68.

49 It may seem counterintuitive that increasing health spending in the medium term, to address some of the immediate apparent pressures on the NHS, leads to greater long-term fiscal pressures. But the June announcement can be interpreted as a crystallisation of medium- and long-term risks that we highlighted in our 2017 *Fiscal risks report*, namely that the medium-term path set out before the announcement would turn out to be politically unsustainable. In effect, the Government has now chosen to accommodate most of the demographic and other cost pressures we assume over the next five years, having not previously planned to do so. That will presumably help maintain the quality and quantity of services, but at the cost of greater long-term fiscal pressure if future governments choose to maintain the resulting higher service levels further into the future.

50 Taking all these factors into account, if left unaddressed our latest projections suggest that the primary deficit would rise to 8.6 per cent of GDP and PSND to 282.8 per cent of GDP in 2067-68 and continue rising thereafter. The big picture of upward pressure from health costs and ageing is common to many advanced economies and would still be seen in the UK even if the Government fully finances the June health announcement.

## Chart 3: Decomposition of changes in the net debt projection since FSR 2017




Source: OBR

## Table 1: Changes in the primary balance and net debt since *FSR* 2017

| | Per cent of GDP | | | |
|---|---|---|---|---|
| | Primary deficit | | Debt | |
| | 2022-23 | 2067-68 | 2022-23 | 2067-68 |
| FSR 2017 | -0.6 | 7.4 | 80.3 | 241.2 |
| Modelling | 0.0 | 0.0 | 0.0 | 8.2 |
| Classification | 0.0 | 0.0 | -3.4 | -3.7 |
| Demographics | 0.0 | 0.2 | 0.0 | 8.9 |
| Forecast changes up to March 2018 EFO | 0.0 | 0.0 | 1.0 | 1.3 |
| FSR 2018 pre-policy changes | -0.6 | 7.5 | 77.9 | 255.9 |
| Long-term policy | 0.0 | -0.4 | 0.0 | -31.0 |
| June health spending | 0.9 | 1.5 | 2.3 | 57.9 |
| FSR 2018 | 0.3 | 8.6 | 80.2 | 282.8 |

51 Needless to say, there are huge uncertainties around any projections that extend this far into the future. Small changes to underlying assumptions can have large effects on the projections once they have been cumulated across many decades. We therefore test the sensitivity of the baseline projection using several different scenarios.

52 The eventual increase in PSND would be greater than in our baseline projection if long-term interest rates turned out to be higher relative to economic growth, if the age structure of the population was older, or if net inward migration (which is concentrated among people of working age) was lower than in our baseline projection.

53 Given the importance of health spending in the long-term challenge to fiscal sustainability, the pace at which non-demographic pressures push spending up is an important assumption. Faster or slower excess cost growth would see health spending rise by more or

less than in our baseline projection – by +2.5/-2.1 per cent of GDP in the ±0.5 percentage point sensitivity analyses we present.

54 Over a shorter time horizon, the Government has set itself an objective of balancing the budget by the middle of the next decade. Our projections suggest that this will be challenging in the face of ageing pressures on health, social care and state pensions spending, and if non-demographic pressures on health spending continue at close to their recent pace. That would be true even if tax and benefit thresholds were uprated in line with inflation rather than earnings beyond our medium-term forecast horizon, boosting tax receipts through fiscal drag and reducing welfare spending through the erosion of the average awards relative to average earnings.

## Summary indicators of fiscal sustainability

55 In our baseline projections, and under the variants we construct, on current policy we would expect the budget deficit to widen significantly over the long term, putting public sector net debt on a rising trajectory as a share of national income. This would not be sustainable.

56 Summary indicators of sustainability can be used to illustrate the scale of the challenge more rigorously and to quantify the tax increases and/or spending cuts necessary to return the public finances to different definitions of sustainability. We focus on a measure of sustainability that asks how large a permanent spending cut or tax increase would be necessary to move public sector net debt to a particular desired level at a particular chosen date. This is referred to as the 'fiscal gap'.

57 There is no consensus on what an optimal level for the public debt to GDP ratio would be. So, for illustration, we calculate the additional fiscal tightening necessary from 2022-23 to return PSND to 20, 40 or 60 per cent of GDP at the end of our projections in 2067-68. In practice, given that expenditure pressures in our projections build up gradually over time, a phased fiscal adjustment might be considered a more realistic illustration.

58 Under our baseline projection, a once and for all policy tightening of 5.2 per cent of GDP in 2023-24 (£111 billion in today's terms) would see the debt ratio come in at 40 per cent of GDP in 2067-68. But this is less than the 8.6 per cent of GDP required to stabilise debt over the longer term, so the debt ratio would continue rising beyond the target date. Tightening policy by 1.9 per cent of GDP a decade would see the debt ratio fall more slowly to begin with, but the overall tightening would be large enough to stabilise the debt ratio at around the target level and prevent it from taking off again.

59 These estimates are slightly larger than in our previous report, as the effect of higher medium-term health spending more than offsets the long-term policy tightening due to faster SPA rises and dropping the Dilnot reforms to adult social care. Targeting debt ratios of 20 and 60 per cent of GDP would require larger and smaller adjustments respectively.

# Annex B

# Fiscal impact of policy decisions

The tables in this annex show the fiscal impact of policy decisions taken at Spring Budget 2020.

## Table B.1: Spring Budget 2020 policy decisions (£ million) [1]

| | | Head[2] | 2019 -20 | 2020 -21 | 2021 -22 | 2022 -23 | 2023 -24 | 2024 -25 |
|---|---|---|---|---|---|---|---|---|
| Investing in excellent public services | | | | | | | | |
| | *Spending review* | | | | | | | |
| 1 | Spending Round 2019 and set resource envelope for the Comprehensive Spending Review 2020 | Spend | -2,530 | - 12,600 | - 27,225 | - 32,095 | - 36,085 | - 42,320 |
| 2 | Delivering public service commitments including on health, schools, criminal justice system (resource spending)[3] | Spend | 0 | -1,430 | -2,685 | -2,795 | -2,825 | - |
| 3 | EU contributions: benefit from contributions no longer paid and customs duties retained | Spend | 0 | +4,34 0 | +4,99 0 | +7,13 0 | +11,2 50 | +14,6 05 |
| 4 | Farm Support: domestic direct payments[4] | Spend | 0 | -2,710 | - | - | - | - |
| | *Delivering excellent services* | | | | | | | |
| 5 | National Health Service: 40 hospitals, diagnostics, operational capital[5] | Spend | 0 | -1,065 | - | - | - | - |
| 6 | Immigration Health Surcharge: increase to £624 with £470 rate for children and extend to EEA nationals | Tax | 0 | +150 | +355 | +355 | +360 | +355 |
| 7 | Pensions: increase annual allowance taper threshold and adjusted income limit, reduce minimum annual allowance | Tax | 0 | -180 | -315 | -450 | -560 | -670 |
| 8 | Prisons: maintenance[4,5] | Spend | 0 | -175 | - | - | - | - |
| 9 | Policing: counter terrorism[4] | Spend | 0 | -80 | - | - | - | - |
| 10 | Safer Streets Fund: CCTV and street lighting[4,6] | Spend | 0 | -15 | - | - | - | - |
| 11 | Public Works Loan Board: increase main rate, with reduced rates for social housing and infrastructure | Spend | +105 | +60 | +175 | +205 | +270 | +325 |
| Supporting people and families | | | | | | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | *Tax* | | | | | | | |
| 12 | National Insurance: increase Primary Threshold and Lower Profit Limit to £9,500 in April 2020 | Tax | * | -2,110 | -2,185 | -2,360 | -2,370 | -2,370 |
| 13 | Fuel duty: freeze for 2020-21 | Tax | 0 | -525 | -530 | -540 | -555 | -560 |
| 14 | Alcohol Duty: freeze all rates for 2020-21[10] | Tax | -40 | -285 | -295 | -305 | -310 | -320 |
| 15 | VAT: zero rate e-publications | Tax | 0 | -60 | -175 | -185 | -190 | -200 |
| 16 | National Insurance: NICs holiday for employers of veterans in first year of civilian employment | Tax | 0 | 0 | -15 | -20 | -25 | -25 |
| 17 | VAT: abolish VAT for female sanitary products from January 2021 | Tax | 0 | -5 | -15 | -15 | -15 | -15 |
| 18 | Vehicle Excise Duty: change classification of new motorhomes from 12 March 2020 | Tax | * | -15 | -20 | -25 | -30 | -35 |
| | *Spending* | | | | | | | |
| 19 | Personal Independence Payments: reduce frequency of assessments | Spend | 0 | 0 | 0 | -55 | -75 | -90 |
| 20 | Neonatal Leave: new entitlement to up to 12 weeks paid leave | Spend | 0 | 0 | 0 | 0 | -15 | -15 |
| 21 | Housing Benefit: further shared accommodation rate exemptions | Spend | 0 | 0 | 0 | 0 | -10 | -15 |
| 22 | Rough sleeping[4,5] | Spend | 0 | -60 | - | - | - | - |
| Backing business | | | | | | | | |
| 23 | Capital Allowances: increase structures and buildings allowance rate to 3% | Tax | -15 | -90 | -165 | -210 | -260 | -295 |
| 24 | Research and Development Expenditure Credit: increase rate to 13% | Spend | 0 | * | -170 | -275 | -300 | -310 |
| 25 | Employment Allowance: increase from £3,000 to £4,000 | Tax | 0 | -445 | -455 | -465 | -470 | -475 |
| 26 | Business Rates: increase retail discount to 50%, and extend to cinemas and music venues for 2020-21 | Tax | +10 | -270 | -15 | 0 | 0 | 0 |
| 27 | Business Rates: £1,000 discount for pubs with rateable value of less than £100,000 for 2020-21 | Tax | * | -20 | * | 0 | 0 | 0 |
| 28 | Corporation Tax: relief for pre-2002 intangible fixed assets | Tax | -5 | -25 | -60 | -95 | -140 | -185 |
| 29 | Enterprise: business productivity and locally delivered business support | Spend | 0 | -20 | - | - | - | - |
| Levelling up and getting Britain building | | | | | | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| 30 | Spending Round 2019 and set capital envelope for the Comprehensive Spending Review 2020 | Spend | 0 | -2,450 | -13,690 | -14,465 | -13,610 | -22,500 |
| 31 | Delivering investment commitments including on transport, health, justice, education, R&D (capital spending)[7] | Spend | 0 | -3,290 | -4,315 | -6,160 | -8,150 | - |
| 32 | Housing: building safety fund[4,5] | Spend | 0 | -1,215 | - | - | - | - |
| 33 | Housing: brownfield housing fund[5] | Spend | 0 | -95 | - | - | - | - |
| 34 | Culture: cultural investment fund, parklife, national museums maintenance[4,5] | Spend | 0 | -95 | - | - | - | - |
| Growing a greener economy | | | | | | | | |
| 35 | Ultra low emission vehicle grants[4,5] | Spend | 0 | -140 | - | - | - | - |
| 36 | Air Quality[5] | Spend | 0 | -175 | - | - | - | - |
| 37 | Renewable Heat Incentive: extend | Spend | 0 | 0 | -10 | -30 | -35 | -35 |
| 38 | Plastic Packaging Tax: 30% recycled content threshold and £200 per tonne | Tax | 0 | 0 | 0 | +240 | +235 | +220 |
| 39 | Red Diesel: remove relief for sectors other than rail, home heating and agriculture | Tax | 0 | 0 | +15 | +1,575 | +1,640 | +1,645 |
| 40 | Climate Change Levy: two year extension to climate change agreement scheme and open to new entrants | Tax | 0 | * | -5 | -5 | -190 | -190 |
| 41 | Climate Change Levy: increase gas rate in 2022-23 and 2023-24, freeze liquid petroleum gas and other commodities | Tax | 0 | 0 | 0 | +130 | +260 | +270 |
| 42 | Capital Allowances for Business Cars: extend first year allowance on zero emission cars and raise eligibility criteria | Tax | 0 | * | -5 | +10 | +70 | +110 |
| 43 | Carbon Price Support: freeze for 2021-22 | Tax | 0 | 0 | -20 | -15 | -15 | -15 |
| 44 | Vehicle Excise Duty: exempt zero emission vehicles from the expensive car supplement | Tax | 0 | -10 | -15 | -20 | -30 | -45 |
| A fair and sustainable tax system | | | | | | | | |
| 45 | Corporation Tax: maintain at 19% | Tax | +930 | +4,635 | +6,120 | +6,680 | +7,075 | +7,500 |
| 46 | Capital Gains Tax: reduce the lifetime limit in entrepreneurs' relief to £1,000,000 | Tax | +5 | +215 | +1,120 | +1,470 | +1,670 | +1,820 |
| 47 | Stamp Duty Land Tax: 2% non-UK resident surcharge | Tax | 0 | +250 | -355 | +35 | +105 | +105 |
| 48 | Tobacco Duty: extend RPI plus 2ppt escalator and additional 4ppt for hand rolling tobacco in 2020-21 | Tax | +5 | +30 | +35 | +30 | +15 | +5 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| 49 | Income Tax: top slicing relief amendments | Tax | 0 | * | -15 | -15 | -15 | -20 |
| 50 | Digital Services Tax: technical changes | Tax | +65 | -5 | * | * | * | +70 |
| 51 | Corporate Capital Loss Restriction: companies in liquidation | Tax | * | * | -5 | -5 | -5 | -5 |
| 52 | Aggregates Levy: freeze for 2020-21 | Tax | 0 | -10 | -10 | -10 | -10 | -10 |
| 53 | Heavy Goods Vehicle VED and Levy: freeze in 2020-21 | Tax | 0 | -10 | -10 | -10 | -10 | -10 |
| 54 | Car Fuel Benefit: increase by CPI in 2020-21 | Tax | 0 | +5 | +5 | +5 | +5 | +5 |
| 55 | Savings: maintain £20,000 limit for adult ISA in 2020-21 | Tax | 0 | * | * | * | * | +5 |
| Avoidance, evasion, and unfair outcomes | | | | | | | | |
| 56 | Notification of uncertain tax treatment | Tax | * | +10 | +20 | +40 | +45 | +45 |
| 57 | Tackling abuse in the construction industry scheme | Tax | 0 | 0 | 0 | +20 | +20 | +15 |
| 58 | Conditionality: hidden economy | Tax | 0 | 0 | +5 | +35 | +50 | +65 |
| 59 | Investment in HMRC to improve tax compliance | Tax | +55 | +280 | +855 | +1,065 | +1,075 | +595 |
| 60 | Research and Development PAYE Cap: delay by one year and updated design | Spend | 0 | 0 | -60 | -130 | -65 | -35 |
| 61 | Housing Benefit: investment in fraud detection by Local Authorities | Spend | 0 | +115 | +140 | +125 | +105 | +60 |
| Financial transactions | | | | | | | | |
| 62 | Public sector net borrowing impact of financial transaction changes[8] | Spend | +2,160 | +2,530 | +2,900 | +3,155 | +990 | +985 |
| Previously announced policy decisions | | | | | | | | |
| 63 | Independent Loan Charge Review: implementation of the recommendations | Tax | -30 | -305 | -245 | -70 | -70 | -25 |
| 64 | Windrush: tax exemption for compensation payments | Tax | * | -5 | -5 | * | * | * |
| 65 | Protecting Your Taxes in Insolvency: delay start date to December and extend to Northern Ireland | Tax | -5 | -30 | -85 | -35 | +5 | +5 |
| 66 | Company Car Tax: temporary reduction for new cars registered from 6 April 2020 | Tax | 0 | -50 | -50 | * | 0 | 0 |
| 67 | Stamp Tax on Shares: connected company transfers | Tax | 0 | +5 | +5 | +5 | +5 | +5 |
| 68 | VAT: change start date for reverse charge for building and constructions services | Tax | -85 | -60 | +20 | +15 | 0 | 0 |
| 69 | Business Rates Retention Pilots: 2020-21 pilots in Devolution Deal | Spend | 0 | -150 | +45 | 0 | 0 | 0 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | areas and the Greater London Authority | | | | | | | |
| 70 | Negative Revenue Support Grant: eliminate in 2020-21 | Spend | 0 | -65 | 0 | 0 | 0 | 0 |
| 71 | Communities: youth investment fund[4,5] | Spend | 0 | -80 | - | - | - | - |
| 72 | Welfare: restrict EEA migrants' access to non-contributory benefits for first five years in UK from January 2021 | Spend | 0 | * | +5 | +25 | +50 | +80 |
| 73 | Child Benefit and Child Tax Credits: end exporting for children outside the UK from January 2021 | Spend | 0 | * | * | * | +5 | +5 |
| 74 | Universal Credit: delay surplus earnings threshold reduction by one year | Spend | 0 | -75 | 0 | 0 | 0 | 0 |
| 75 | Universal Credit: additional support for claimants transferring to pension credit | Spend | 0 | -5 | -10 | -10 | -15 | -25 |
| 76 | Universal Credit: changes to severe disability premium regulations | Spend | -10 | -5 | -5 | * | * | 0 |
| | Total policy decisions[9] | | +605 | -17,900 | -36,430 | -38,530 | -41,150 | -41,920 |
| | Total spending policy decisions[9] | | -355 | -19,255 | -40,185 | -45,640 | -48,780 | -49,440 |
| | *Of which current* | | *-2,545* | *-13,765* | *-24,910* | *-27,860* | *-27,680* | *-27,660* |
| | *Of which capital* | | *+2,190* | *-5,490* | *-15,275* | *-17,775* | *-21,100* | *-21,780* |
| | Total tax policy decisions[9] | | +960 | +1,355 | +3,755 | +7,110 | +7,625 | +7,520 |

* Negligible.

[1] Costings reflect the OBR's latest economic and fiscal determinants.

[2] Many measures have both tax and spend impacts. Measures are identified as tax or spend on the basis of their largest impact.

[3] The overall spending level in 2024-25 has been adjusted for the costs of these measures. Settlements for 2024-25 will be set out at the Spending Review after the Comprehensive Spending Review 2020.

[4] The overall resource spending envelope has been adjusted to include funding for this measure in future years. Settlements over the period 2020-21 to 2023-24 will be set out in full at the Comprehensive Spending Review 2020.

[5] These costs are additional capital spending in 2020-21. Future profiles and total programme costs for some specific programmes are detailed elsewhere in the document. Settlements beyond 2020-21 will be set out in full at the Comprehensive Spending Review 2020.

[6] Safer Streets Fund: There is a total of £25m in this Fund, of which £10m is funded from the Home Office settlement.

[7] Departments have existing 2020-21 capital budgets. Some additions were made to 2020-21 capital budgets at the Spending Review 2019 and further additions are made at this Budget. Years beyond 2021-22 represent the overall capital envelope, which will be allocated to departments at the Comprehensive Spending Review 2020. Some specific capital allocations are set out throughout this document.

[8] Further details on financial transactions is set out in the financial transaction table.

[9] Totals may not sum due to rounding.

[10] The modelling for this measure was corrected after this table was finalised. The accompanying published costing note contains the updated impacts on the public finances.

Source: Spring Budget 2020

## Table B.2: Measures announced at Budget 2018 or earlier that will take effect from March 2020 or later (£ million)[a]

| | | Head[2] | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|---|
| Measures announced at Budget 2018 | | | | | | | | |
| | *Spending review* | | | | | | | |
| a | Universal Credit: additional support for transition | Spend | -90 | -125 | -140 | -130 | -165 | -185 |
| b | Universal Credit: revised implementation schedule | Spend | -95 | +310 | +750 | +545 | -30 | -100 |
| c | Industrial Injuries Disablement Benefit: include Dupuytren's contracture | Spend | 0 | -5 | -5 | -5 | -5 | -5 |
| d | Business Rates: public lavatories relief from 2020-21 | Tax | 0 | -5 | -5 | -5 | -5 | -5 |
| e | Digital Services Tax | Tax | +5 | +285 | +390 | +425 | +460 | +440 |
| f | Off-payroll Working: extend reforms to private sector in 2020-21, excluding small businesses | Tax | -150 | +1190 | +705 | +710 | +800 | +870 |
| g | Corporation Tax: restrict use of carried forward capital losses from 2020-21 | Tax | +30 | +130 | +170 | +165 | +150 | +140 |
| h | Private Residence Relief: reform lettings relief and final period exemption from 2020-21 | Tax | +10 | +55 | +125 | +140 | +150 | +155 |
| i | VAT Registration Threshold: maintain at £85,000 for a further two years | Tax | 0 | +40 | +95 | +125 | +135 | +135 |
| j | Employment Allowance: restrict to businesses below a £100,000 employer NICs threshold from 2020-21 | Tax | 0 | +235 | +270 | +305 | +340 | +345 |
| k | Climate Change Levy: move towards equalised gas and electricity rates | Tax | 0 | +40 | +60 | +65 | +85 | +90 |
| l | Alcohol Duty: ban post duty point dilution | Tax | +60 | -15 | +65 | +70 | +70 | +70 |
| m | R&D Tax Credits: preventing abuse of the SME payable credit | Spend | 0 | 0 | +60 | +165 | +185 | +175 |
| n | Withheld Taxes: protecting your taxes in insolvency and tackling abuse | Tax | +10 | +75 | +185 | +230 | +225 | +220 |
| o | Capital Allowances: discontinue enhanced allowances for energy and water-efficient equipment | | | | | | | |
| Measures announced Autumn Budget 2017 | | Tax | +10 | +50 | +85 | +70 | +65 | +65 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| p | Non-resident property income: move from Income Tax to Corporation Tax | Tax | 0 | +760 | -295 | +5 | 0 | +5 |
| q | Capital Gains Tax payment window reduction: delay to April 2020 | Tax | -985 | +770 | +190 | +10 | +5 | 0 |
| Measure announced Autumn Budget 2016 | | | | | | | | |
| r | Company Car Tax: reforms to incentivise ULEVs | Tax | 0 | -25 | -65 | -100 | -160 | -205 |
| Measure announced Spring Budget 2016 | | | | | | | | |
| s | Corporation Tax: reduce to 17% in April 2020 (relative to 18%) | Tax | -475 | -2350 | -3120 | -3420 | -3640 | -3875 |

* Negligible
[1] Costings reflect the OBR's latest economic and fiscal determinants.
[2] Many measures have both tax and spend impacts. Measures are identified as tax or spend on the basis of their largest impact.

# Annex C
# Supplementary data tables

Information in these tables these tables is consistent with the OBR's March 2020 'Economic and fiscal outlook' (EFO) and supplementary tables, unless otherwise noted. The OBR's supplementary tables are available here.

Any HM Treasury calculations are derived from and consistent with published sources. Further details of outturn statistics drawn from Budget 2020 or EFO can be found in the data sources documents on the HMT and OBR websites respectively.

## Table A.1: Macroeconomic Prospects

| | Level[a] | Rate of Change | | | | | |
|---|---|---|---|---|---|---|---|
| | 2019 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
| Real GDP | 2089.4 | 1.4 | 1.1 | 1.8 | 1.5 | 1.3 | 1.4 |
| Nominal GDP | 2214.9 | 3.3 | 3.1 | 3.8 | 3.7 | 3.4 | 3.5 |
| Private consumption expenditure[b] | 1366.1 | 1.3 | 1.1 | 1.2 | 1.2 | 1.4 | 1.4 |
| Government consumption expenditure | 397.9 | 3.6 | 3.7 | 2.8 | 2.1 | 1.9 | 2.2 |
| Gross fixed capital formation | 349.9 | 0.4 | -0.8 | 3.4 | 2.9 | 2.0 | 1.8 |
| Changes in inventories and net acquisition of valuables (% of GDP)[c] | -0.1 | 0.0 | -0.1 | 0.1 | 0.0 | 0.0 | 0.0 |
| Exports of goods and services | 632.2 | 3.7 | -0.6 | -0.5 | -0.6 | -1.1 | -1.0 |
| Imports of goods and services | 655.9 | 3.6 | -0.2 | 0.4 | 0.2 | 0.2 | 0.2 |
| Contributions to real GDP Growth | | | | | | | |
| Final domestic demand | - | 1.5 | 1.3 | 1.9 | 1.7 | 1.6 | 1.7 |
| Changes in inventories and net acquisition of valuables | - | 0.0 | -0.1 | 0.1 | 0.0 | 0.0 | 0.0 |
| External balance of goods and services | | 0.0 | -0.1 | -0.3 | -0.2 | -0.4 | -0.3 |

a Pounds sterling, billion. (In 2016 prices for real GDP)

b Includes households and non-profit institutions serving households.

c Rate of change of changes in inventories and net acquisition of valuables is given as the percentage point year-on-year change.

## Table A.2: Price Developments

| | Level | Rate of Change | | | | | |
|---|---|---|---|---|---|---|---|
| | 2019 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
| GDP deflator | 106.0 | 1.8 | 2.0 | 2.0 | 2.2 | 2.1 | 2.1 |
| Private consumption deflator | 105.4 | 1.3 | 1.2 | 1.8 | 2.1 | 2.1 | 2.0 |
| HICP[a] | 107.8 | 1.8 | 1.4 | 1.8 | 2.1 | 2.1 | 2.0 |
| Public consumption deflator | 105.0 | 1.8 | 2.5 | 2.9 | 2.1 | 1.9 | 1.9 |
| Investment deflator | 107.7 | 3.5 | 1.7 | 1.3 | 1.8 | 1.7 | 2.1 |
| Export price deflator (goods and services) | 109.0 | 1.2 | -3.2 | -1.2 | 0.2 | 0.4 | 0.5 |
| Import price deflator (goods and services) | 109.6 | 1.1 | -2.8 | -1.1 | 0.0 | 0.3 | 0.4 |

[a] The UK's Harmonised Index of Consumer Prices (HICP) is the Consumer Price Index (CPI).

## Table A.3: Labour Market Developments

| | Level | Rate of Change | | | | | |
|---|---|---|---|---|---|---|---|
| | 2019 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
| Employment, persons (millions)[a] | 32.8 | 1.1 | 0.5 | 0.4 | 0.4 | 0.3 | 0.3 |
| Employment, hours worked[b] | 1052.1 | 1.4 | 0.1 | 0.6 | 0.3 | 0.2 | 0.2 |
| Unemployment rate (%)[c] | 3.8 | -0.3 | 0.0 | 0.0 | 0.1 | 0.1 | 0.1 |
| Labour productivity, persons[d] | 63703.7 | 0.3 | 0.5 | 1.4 | 1.1 | 1.0 | 1.1 |
| Labour productivity, hours worked[e] | 38.2 | 0.0 | 0.9 | 1.2 | 1.2 | 1.1 | 1.2 |
| Compensation of employees[f] | 1098.8 | 4.3 | 4.2 | 4.0 | 3.7 | 3.4 | 3.2 |
| Compensation per employee[g] | 39482.3 | 3.6 | 3.9 | 3.7 | 3.5 | 3.2 | 3.0 |

a All aged 16 and over.

b Millions per week.

c ILO measure, all aged 16 and over. Rate of change is percentage point year on year change.

d GDP per worker, pounds sterling.

e GDP per hour, pounds sterling.

f Pounds sterling, billion

g Pounds per worker

## Table A.4: Sectoral Balances

| % of GDP | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| Net lending/borrowing vis-à-vis the rest of the world | 4.8 | 3.1 | 3.9 | 4.0 | 4.0 | 4.1 | 4.1 |
| *of which:* | | | | | | | |
| - Balance on goods and services | -2.2 | -0.6 | -1.6 | -1.7 | -1.8 | -2.1 | -2.2 |
| - Balance of primary incomes and transfers | -2.6 | -2.5 | -2.2 | -2.3 | -2.1 | -2.0 | -1.8 |
| - Capital account | -0.1 | -0.1 | -0.1 | -0.1 | -0.1 | -0.1 | -0.1 |

## Table A.5: General government budgetary prospects

| | £ billion | % of GDP | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | | |
| | 2018-19 | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Net lending by subsector | | | | | | | | |
| General government[a] | 38.9 | 1.8 | 2.2 | 2.5 | 3.1 | 2.6 | 2.4 | 2.4 |
| Central government | 33.7 | 1.6 | 1.8 | 2.0 | 2.7 | 2.2 | 2.0 | 2.0 |
| Local government | 5.2 | 0.2 | 0.5 | 0.5 | 0.4 | 0.4 | 0.4 | 0.3 |
| General government | | | | | | | | |
| Total revenue | 794.5 | 36.7 | 36.7 | 36.9 | 36.8 | 37.2 | 37.4 | 37.3 |
| Total expenditure | 833.4 | 38.5 | 38.9 | 39.3 | 39.9 | 39.8 | 39.8 | 39.6 |
| Net borrowing[a] | 38.9 | 1.8 | 2.2 | 2.5 | 3.1 | 2.6 | 2.4 | 2.4 |
| Interest expenditure | 49.5 | 2.3 | 2.2 | 2.0 | 2.0 | 1.9 | 1.8 | 1.7 |
| Primary balance[b] | 10.5 | 0.5 | 0.0 | -0.5 | -1.1 | -0.6 | -0.6 | -0.6 |
| Selected components of revenue | | | | | | | | |
| Taxes on production and imports | 281.4 | 13.0 | 13.0 | 12.9 | 13.0 | 13.1 | 13.0 | 13.0 |
| Taxes on income and wealth | 260.0 | 12.0 | 11.8 | 12.1 | 12.2 | 12.4 | 12.5 | 12.6 |
| Capital taxes | 5.5 | 0.3 | 0.2 | 0.2 | 0.2 | 0.3 | 0.3 | 0.3 |
| Social contributions | 137.3 | 6.3 | 6.5 | 6.5 | 6.6 | 6.6 | 6.6 | 6.7 |
| Other | 110.4 | 5.1 | 5.1 | 5.1 | 4.8 | 4.9 | 5.0 | 4.8 |
| Total revenue | 794.5 | 36.7 | 36.7 | 36.9 | 36.8 | 37.2 | 37.4 | 37.3 |
| Selected components of expenditure | | | | | | | | |
| Current expenditure | 400.7 | 18.5 | 19.1 | 19.6 | 19.9 | 20.0 | 20.1 | 20.2 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| on goods and services | | | | | | | | |
| Net social benefits | 242.4 | 11.2 | 10.7 | 10.6 | 10.5 | 10.5 | 10.5 | 10.5 |
| Interest expenditure | 49.5 | 2.3 | 2.2 | 2.0 | 2.0 | 1.9 | 1.8 | 1.7 |
| Subsidies | 20.1 | 0.9 | 1.2 | 1.2 | 1.2 | 1.1 | 1.1 | 1.1 |
| Gross fixed capital formation | 57.4 | 2.6 | 2.7 | 2.8 | 3.0 | 3.1 | 3.1 | 3.1 |
| Other | 63.4 | 2.9 | 3.0 | 3.2 | 3.3 | 3.2 | 3.1 | 3.0 |
| Total expenditure | 833.4 | 38.5 | 38.9 | 39.3 | 39.9 | 39.8 | 39.8 | 39.6 |

a Treaty deficit

b General government net borrowing less interest expenditure

### No-policy change projections and amounts to be excluded from the expenditure benchmark

| | £billion | % of GDP | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Outturn | | | Forecast | | | | |
| | 2018-19 | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Total revenue at unchanged policies[a] | 794.5 | 38.1 | 37.6 | 37.9 | 38.1 | 38.4 | 38.6 | 38.6 |
| Expenditure on EU programmes fully matched by EU fund revenue[b] | 5.1 | 0.2 | 0.3 | 0.3 | | | | |
| Cyclical unemployment benefit expenditure[c] | 1.7 | 0.1 | 0.0 | | | | | |
| Discretionary revenue measures[d] | - | - | 0.1 | 0.2 | 0.1 | 0.1 | 0.0 | 0.0 |

a General government total revenue less discretionary revenue measures between Budget 2014 and Spring Budget 2020 (consistent with the OBR's Economic and fiscal outlook).

b Expenditure on EU programmes fully matched by EU funds revenue is calculated as the 'Public sector receipts from the EU' row from the OBR's Table 2.26 in their March 2019 Economic and fiscal outlook supplementary fiscal tables. This only includes EU receipts that are administered by UK government bodies. (Excludes other private sector receipts that are not administered by UK government bodies.) The EU receipts that are administered by UK government bodies are not netted off current expenditure in the national accounts, because they are deemed to finance spending in the UK by the EU. This data has not been updated since March 2019 Economic and Fiscal Outlook

c Cyclical unemployment benefit expenditure is calculated as is defined as COFOG subfunction 10.5, central government own expenditure on unemployment divided by GDP, and is consistent with Public Expenditure Statistical Analyses 2018 Table 6.4 (which extends to 2019-20). Estimates used for plans data are subject to further revisions by departments. Universal credit additional costs that are not already included against other benefits are not included with the unemployment COFOG category.

d Sum of discretionary revenue measures taken between Budget 2014 and Spring Budget 2020

## Central government expenditure by function[a,b,c]

| | % of GDP | |
|---|---|---|
| | 2017-18 | 2019-20 |
| General public services | 3.5 | 3.2 |
| Defence, public order and safety | 2.6 | 2.7 |
| Economic affairs | 1.8 | 2.2 |
| Environmental protection | 0.2 | 0.2 |
| Housing and community amenities | 0.1 | 0.2 |
| Health | 6.9 | 7.1 |
| Recreation, culture and religion | 0.3 | 0.3 |
| Education | 2.0 | 2.0 |
| Social protection | 10.2 | 10.3 |
| Total expenditure[d] | 29.5 | 29.5 |

a Spending data used consistent with Public Expenditure Statistical Analyses (PESA) 2019, HM Treasury July 2019.

b Central government data taken from PESA 2019 Table 6.4 (which extends to 2019-20)

c Percentage of GDP calculations consistent with March 2020 EFO

d Total expenditure is more than just the sum of the functions, it also includes EU transactions and accounting adjustments

## General government debt developments

| | % of GDP | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | | | Forecast | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Gross debt[a] | 84.1 | 83.2 | 82.9 | 83.2 | 83.3 | 83.3 | 83.0 |
| Change in gross debt ratio | -0.5 | -0.9 | -0.2 | 0.3 | 0.1 | 0.0 | -0.3 |
| Contributions to changes in gross debt | | | | | | | |
| Primary balance[b] | 0.5 | 0.0 | -0.5 | -1.1 | -0.6 | -0.6 | -0.6 |
| Interest expenditure | 2.3 | 2.2 | 2.0 | 2.0 | 1.9 | 1.8 | 1.7 |
| Stock-flow adjustment[c] | -3.3 | -3.1 | -1.7 | -0.7 | -1.2 | -1.3 | -1.4 |
| Implicit interest rate on debt[d] | 2.8 | 2.7 | 2.5 | 2.5 | 2.4 | 2.3 | 2.2 |

a Treaty debt

b General government net borrowing less interest expenditure

c Change in Treaty debt less general government net borrowing

d Interest expenditure as a percentage of Treaty debt in previous year

## Cyclical developments

| | % of GDP | | | | | | |
|---|---|---|---|---|---|---|---|
| | Outturn | Forecast | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
| Net borrowing of general government | 1.8 | 2.2 | 2.5 | 3.1 | 2.6 | 2.4 | 2.4 |
| Interest expenditure | 2.3 | 2.2 | 2.0 | 2.0 | 1.9 | 1.8 | 1.7 |
| Output gap | 0.3 | 0.0 | 0.1 | 0.4 | 0.4 | 0.1 | 0.0 |
| Cyclical budgetary component[a] | -0.1 | 0.0 | 0.0 | -0.2 | -0.3 | -0.1 | 0.0 |
| Cyclically-adjusted balance | -1.9 | -2.3 | -2.5 | -3.3 | -2.8 | -2.5 | -2.4 |
| Cyclically-adjusted primary balance[b] | 0.3 | 0.0 | -0.5 | -1.3 | -0.9 | -0.7 | -0.6 |
| | Outturn | | Forecast | | | | |
| | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
| Real GDP growth (%)[c] | 1.9 | 1.3 | 1.4 | 1.1 | 1.8 | 1.5 | 1.3 |
| Potential GDP growth (%)[c] | 1.2 | 1.4 | 1.2 | 1.4 | 1.4 | 1.5 | 1.6 |

a Treaty deficit less cyclically adjusted treaty deficit

b Cyclically-adjusted treaty deficit less interest expenditure

c Growth in real GDP and growth in potential GDP are expressed in calendar rather than financial years and are calculated on a non-oil basis.

## Divergence from previous update[a]

| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| Real GDP growth (%) | | | | | | | |
| Previous update | 1.4 | 1.2 | 1.5 | 1.6 | 1.6 | 1.6 | |
| Current update | 1.6 | 1.1 | 1.3 | 1.7 | 1.4 | 1.3 | 1.5 |
| Difference | 0.1 | -0.1 | -0.2 | 0.1 | -0.2 | -0.3 | |
| Treaty Deficit[b] | | | | | | | |
| Previous update | 1.2 | 1.4 | 1.1 | 1.1 | 0.7 | 0.6 | |
| Current update | 1.8 | 2.2 | 2.5 | 3.1 | 2.6 | 2.4 | 2.4 |
| Difference | 0.6 | 0.8 | 1.4 | 2.0 | 1.8 | 1.8 | |
| Treaty Debt (%)[c] | | | | | | | |
| Previous update | 85.5 | 83.8 | 82.9 | 82.2 | 81.1 | 80.0 | |
| Current update | 84.1 | 83.2 | 82.9 | 83.2 | 83.3 | 83.3 | 83.0 |
| Difference | -1.4 | -0.6 | 0.1 | 1.1 | 2.2 | 3.3 | |

a Previous update numbers correspond to the OBR's March 2019 Economic and fiscal outlook

b General government net borrowing on a Maastricht basis

c General government gross debt on a Maastricht basis

## Long-term sustainability of public finances[a]

| | % of GDP | | | | | | |
|---|---|---|---|---|---|---|---|
| | Projections | | | | | | |
| | 2018-19 | 2019-20 | 2020-21 | 2030-31 | 2040-41 | 2050-51 | 2060-61 |
| Total expenditure | 38.4 | 38.6 | 38.6 | 40.3 | 44.4 | 49.2 | 54.2 |
| Of which: age-related expenditures[b] | 20.5 | 20.6 | 20.6 | 22.4 | 24.7 | 26.7 | 28.4 |
| State pensions | 5.0 | 5.0 | 4.9 | 5.3 | 6.0 | 6.5 | 6.8 |
| Pensioner benefits | 0.8 | 0.8 | 0.8 | 0.9 | 1.1 | 1.3 | 1.3 |
| Public service pensions | 2.0 | 2.1 | 2.1 | 2.0 | 1.8 | 1.6 | 1.6 |
| Health | 7.1 | 7.3 | 7.4 | 8.8 | 10.3 | 11.7 | 13.0 |
| Long-term care | 1.2 | 1.2 | 1.2 | 1.4 | 1.6 | 1.8 | 1.9 |
| Education | 4.3 | 4.2 | 4.2 | 4.0 | 3.8 | 3.8 | 3.8 |
| Net interest | 1.6 | 1.5 | 1.5 | 1.5 | 3.2 | 5.7 | 8.9 |
| Total revenue | 36.7 | 36.8 | 36.8 | 37.0 | 37.3 | 37.4 | 37.5 |

a Consistent with the central projection in the OBR's July 2018 Fiscal sustainability report

b Sum of pensions, pensioner benefits, public service pensions, health, long-term care and education

## Contingent Liabilities[a]

| £ billion | 2016-17 | 2017-18 |
|---|---|---|
| Total quantifiable contingent liabilities | 182.4 | 192.6 |
| Of which: financial stability interventions | 0.0 | 0.0 |

a Taken from Whole of Governments Accounts- year ended 31 March 2018, HM Treasury, 2019

## Basic assumptions [a]

| | 2018-19 | 2019-20 | 2020-21 | 2021-22 | 2022-23 | 2023-24 | 2024-25 |
|---|---|---|---|---|---|---|---|
| Short-term interest rate (annual average)[b] | 0.8 | 0.8 | 0.8 | 0.8 | 0.8 | 0.9 | 0.9 |
| Long-term interest rate (annual average)[c] | 1.8 | 1.3 | 1.2 | 1.3 | 1.3 | 1.4 | 1.4 |
| Nominal effective exchange rate[d] | 78.4 | 78.6 | 82.8 | 82.6 | 82.4 | 82.2 | 82.1 |
| Exchange rate vis-à-vis the € (annual average) | 1.13 | 1.15 | 1.21 | 1.20 | 1.18 | 1.17 | 1.16 |
| | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
| Oil prices (Brent, USD/barrel) | 70.2 | 62.8 | 55.2 | 54.7 | 55.4 | 56.5 | 57.6 |
| Euro area GDP growth | 1.9 | 1.2 | 1.1 | 1.4 | 1.4 | 1.3 | 1.3 |
| Growth of relevant foreign markets | 2.2 | 1.5 | 2.2 | 3.3 | 3.3 | 3.5 | 3.4 |

a Consistent with March 2020 Economic and Fiscal Outlook

b 3 month sterling interbank rate (LIBOR)

c Weighted average interest rate on conventional gilts

d Trade-weighted sterling

**HM Treasury contacts**

This document can be downloaded from
www.gov.uk

If you require this information in an alternative format or have general enquiries about HM Treasury and its work, contact:

Correspondence Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 5000

Email: public.enquiries@hmtreasury.gov.uk