Office for Budget Responsibility

Local government spending: the national fiscal backdrop

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Chairman

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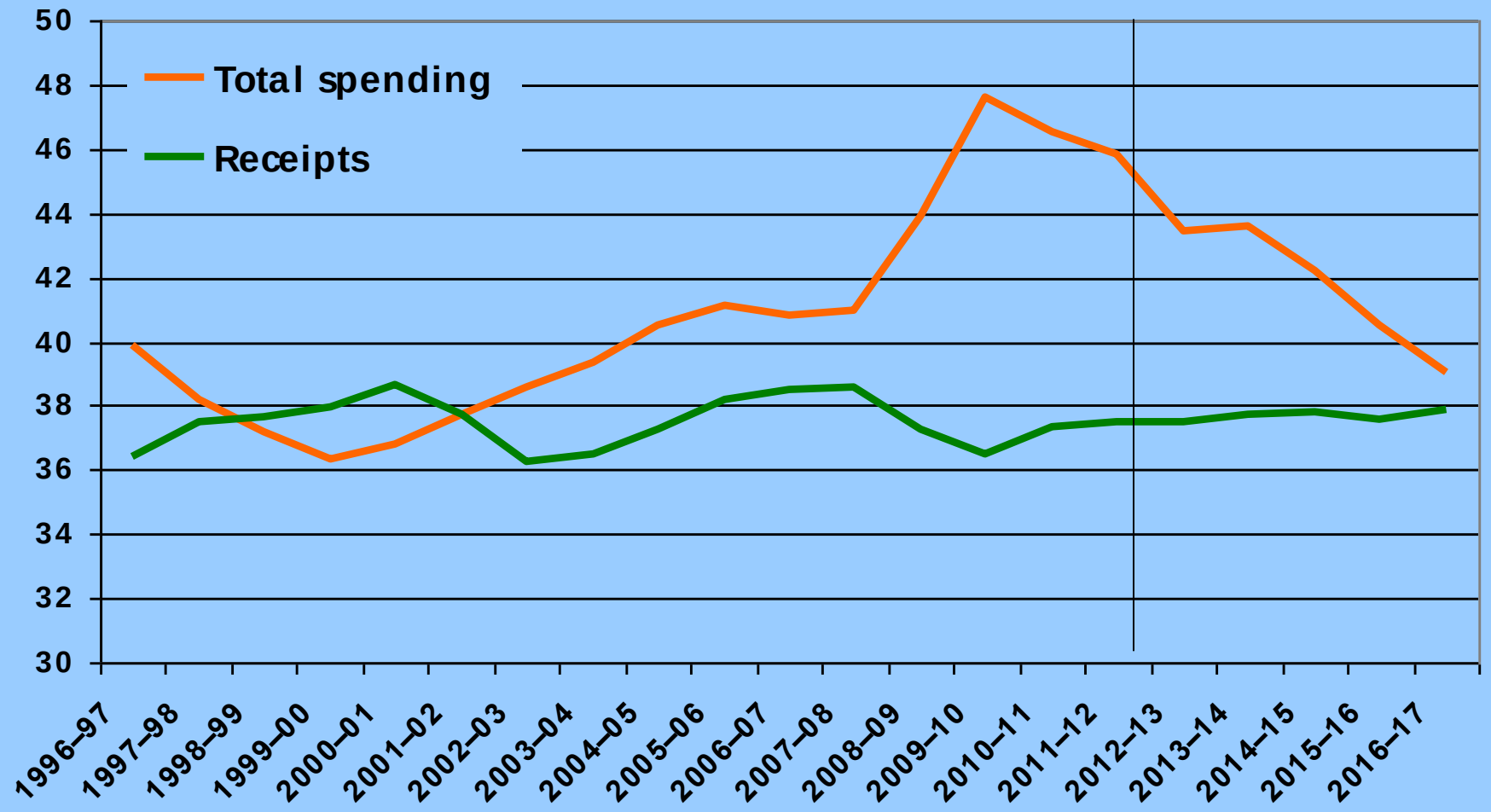
What is the OBR?

- Created in 2010 to provide independent and authoritative analysis of the public finances
- Produces the Budget and Autumn Statement forecasts of the economy and public finances
- Assesses progress against fiscal targets
- Reports on the sustainability of the public finances and the health of the public sector balance sheet
- Scrutinises Treasury costing of policy measures

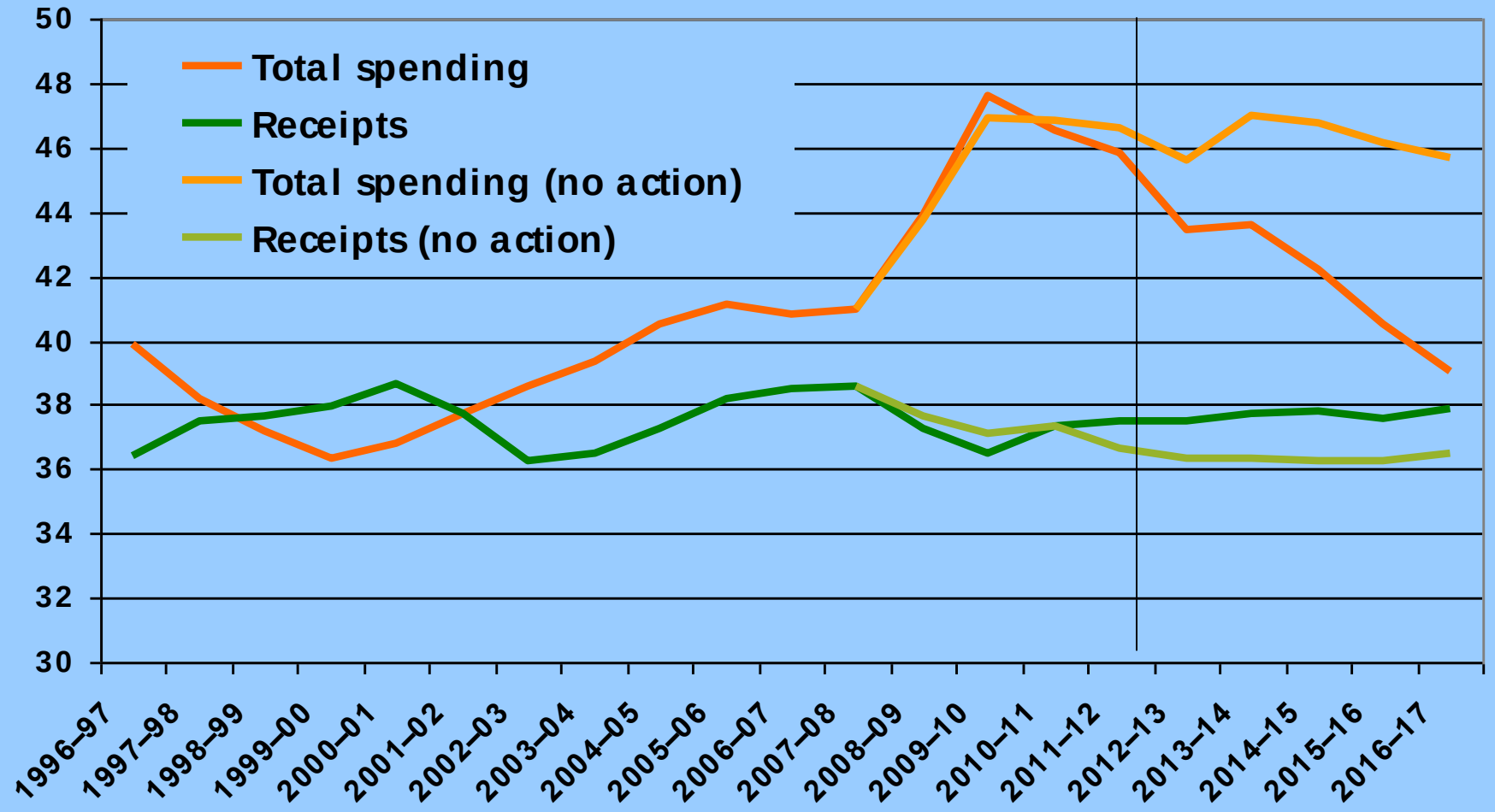
The big picture

- The recession and financial crisis were accompanied by a big increase in government borrowing
- Some of this extra borrowing was temporary
  - Deliberate stimulus measures (e.g. VAT cut)
  - Economic activity running below full capacity
- But some was likely to be persistent (i.e. ‘structural’)
  - Economic potential lower than expected pre-crisis
- Lab and Lib/Con spending cuts and tax increases in effect remove this additional structural borrowing
- But no-one can be sure how much borrowing *is* structural

Public spending and revenues

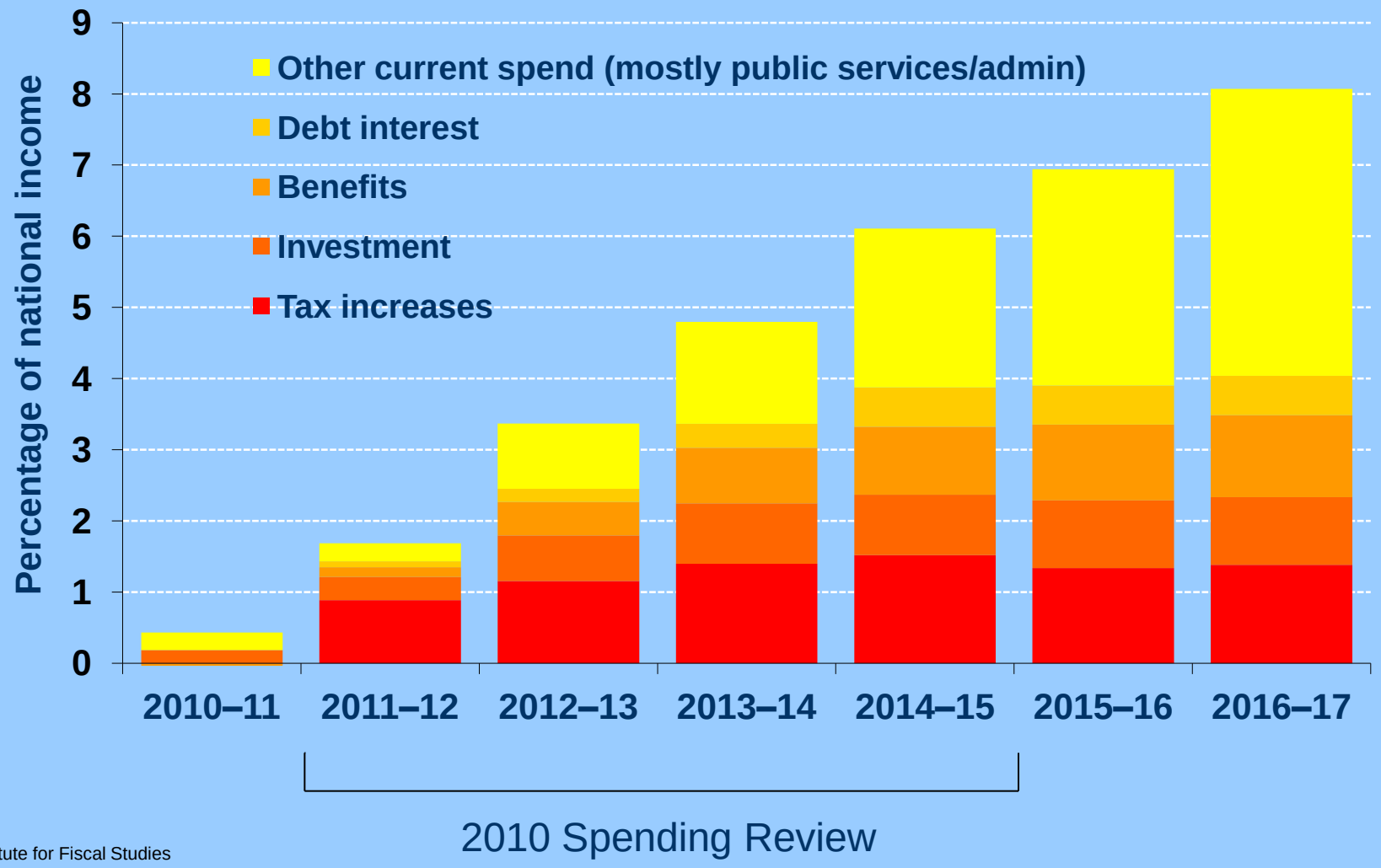


Public spending and revenues



Based on IFS interpretation of consolidation – direct effect only

The fiscal repair job



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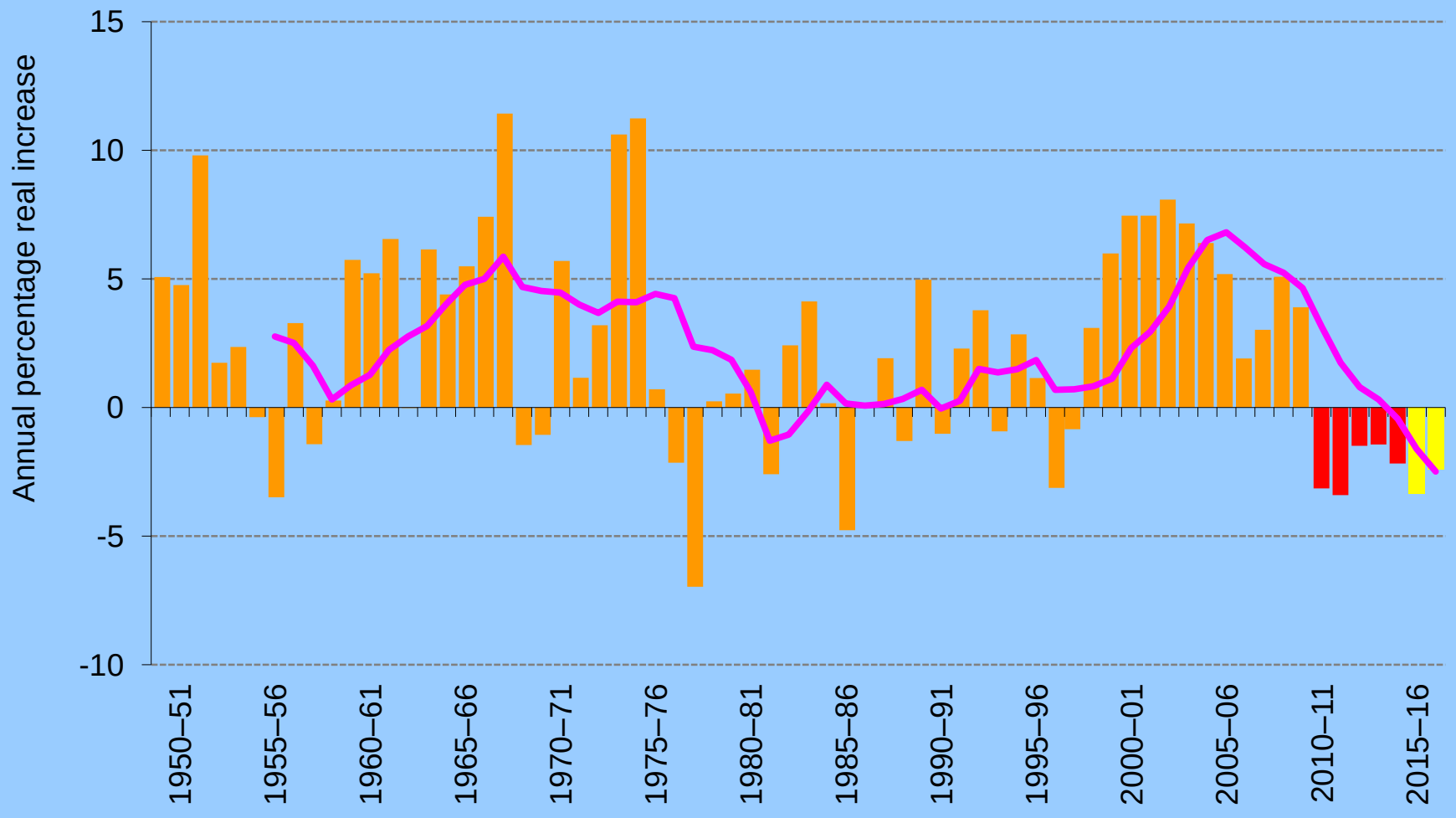
Implies big real public services cuts



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Note: Figure shows total public spending less spending on welfare benefits and debt interest.

Total local authority spending

Cumulative % change in real terms	**Spending review**	**2015-16 & 2016-17**
Central government financed	**–13**	
Of which: DEL (public services)	*–15*	
Of which: AME (benefits/pensions)	*–4*	
Self-financed	**+11**	
Of which: council tax financed	*+2*	
Other (inc national accounts adjusts)	**+3**	
TOTAL	**–8**	
Memo: Total DEL	–11	

- We forecast spending from income plus expected changes in reserves
- Broadest definition of local authority spending
- Adjusted for academies moving from LAs to CG from 2011-12
- Growth in ‘self-financed’ buoyed by transfers to reserves in 2010-11

Total local authority spending

Cumulative % change in real terms	**Spending review**	**2015-16 & 2016-17**
Central government financed	**–13**	**–7**
Of which: DEL (public services)	*–15*	*–8*
Of which: AME (benefits/pensions)	*–4*	*–1*
Self-financed	**+11**	**+3**
Of which: council tax financed	*+2*	*+3*
Other (inc national accounts adjusts)	**+3**	**–3**
TOTAL	**–8**	**–5**
Memo: Total DEL	–11	–7

- Post-SR numbers are top-down OBR assumptions, not plans
- Assumes DEL allocations consistent with total DEL and EFO pay view
- LAs assumed to be hit no harder than CG by DEL cuts
- ‘Other spending’ pattern reflects path of VAT refunds

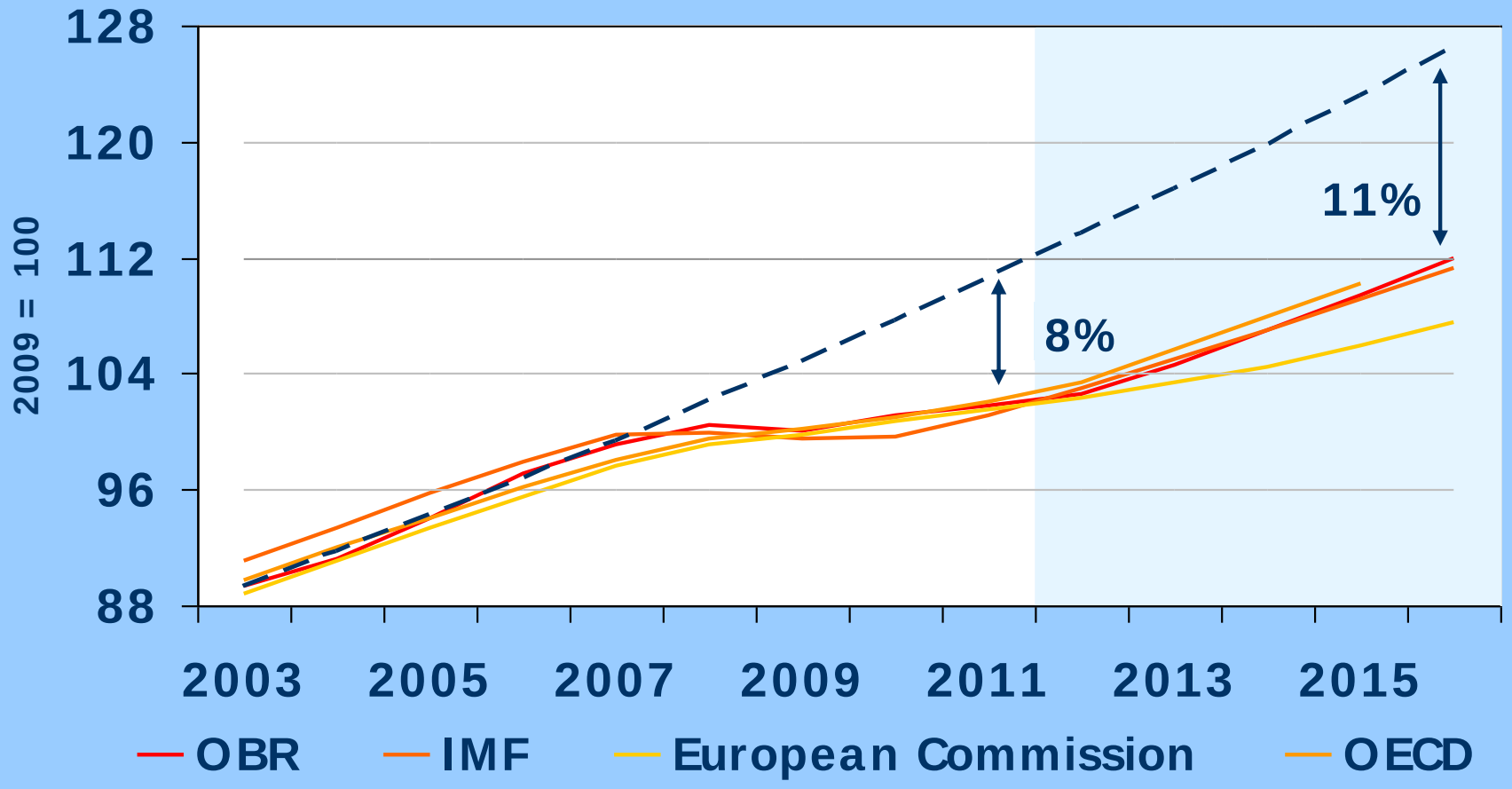
What could change? (1)

- The Government could change its mind about how much fiscal consolidation to do and at what pace
- For example, last November it pencilled in additional current DEL cuts in 2015-16 and 2016-17
- This reflected our view that weaker growth prospects and (crucially) weaker outlook for the productive potential of the economy meant that fiscal targets were more likely than not to be missed
  - Balance structural current budget five years ahead
  - Have debt falling as share of GDP in 2015-16

What could change? (2)

- Weak outturn data and euro drama have pushed down outside growth forecasts
- Temporarily weaker growth (and higher cyclical borrowing) would not make structural current budget significantly harder to balance, but might well make it harder to get debt falling by 2015-16
- Further damage to functioning of banking system (perhaps from disorderly euro-outcome) might hit potential output and increase structural deficit
- But huge uncertainty about the hit to potential GDP

Forecasts of economic potential



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What could change? (3)

- Government could also change its mind about the composition of the consolidation
- For example, in the 2010 Spending Review it shifted some of the burden away from cuts in current spending on public services and towards welfare, with little change to the cuts in capital spending
- Since then the Chancellor has highlighted the welfare / public services spending trade-off again
- Picture will doubtless change from forecast to forecast, but greater clarity in next Spending Review (including relative pain for local/national govt in DELs)