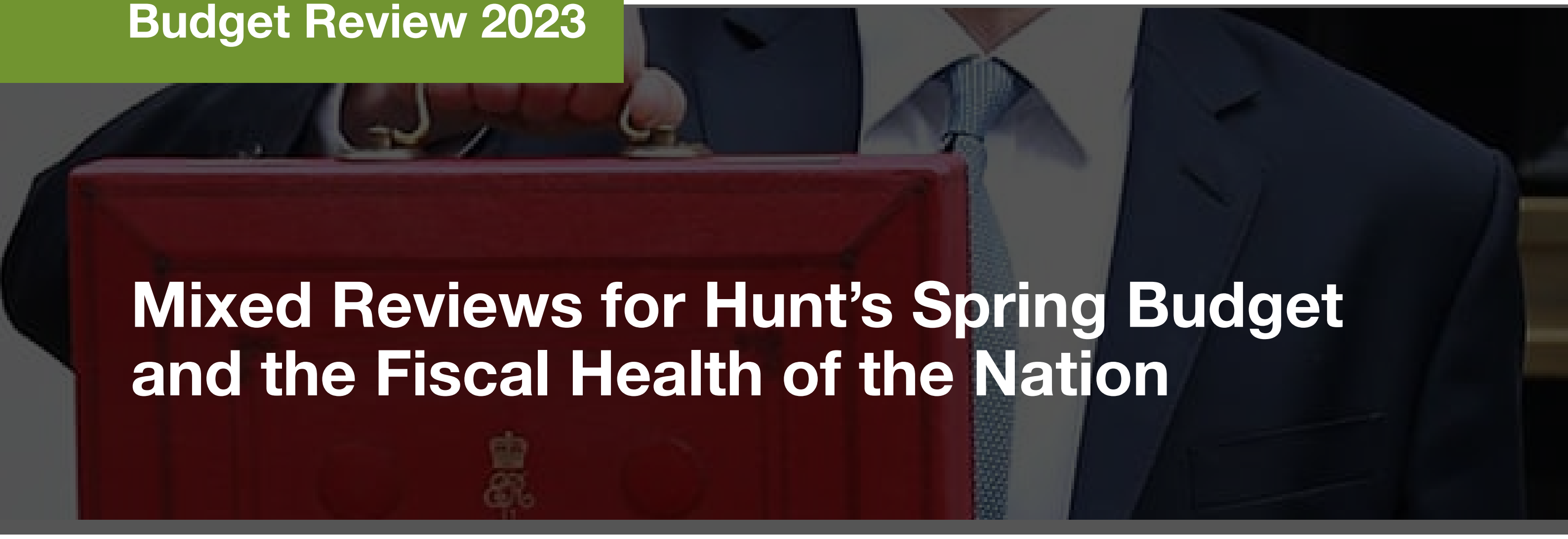
sovereign strategy

Budget Review 2023



Mixed Reviews for Hunt's Spring Budget and the Fiscal Health of the Nation

The country's leading think tanks and policy wonks have given their verdict on Jeremy Hunt's budget and on the health of the nation's finances. As is often the case with economists, it's a mixed picture.

First, the good news: Wholesale gas prices have more than halved over the past six months and the Bank Rate is now expected to peak at 4¼ per cent later this year (rather than the 5 per cent previously forecast). The Office for Budget Responsibility (OBR) – a non-departmental public body funded by the Treasury - has said that the near-term economic downturn is set to be shorter and shallower than feared. Medium-term output is expected to be higher - and the budget deficit and public debt to be lower.

And now the bad news: Although things aren't going to be as bad as originally predicted, they are still going to be bad. Any extra headroom for the Chancellor from tax receipts or economic growth is marginal.

The response from the General Public is also mixed. There is no Budget Bounce in the opinion polls. The Conservatives, although up 4 points to 27% have not drawn away any support from Labour who are up one point at 46%.

Nevertheless, Jeremy Hunt's approach to cautiously balancing the books has been met with a subdued reaction from the international markets – a relief following the tumultuous response to his predecessors ill-fated mini Budget.

Hunt has been constrained by his own fiscal rule of having debt falling as a proportion of the size of economy and his borrowing rule — to have public sector net borrowing below 3% of GDP over the same period. As a result, the tax burden on households and businesses is set to increase. The IFS believes that "a badly designed fiscal rule" is the tail wagging the dog of fiscal policy.

The OBR believes that it is now harder for this Chancellor to deliver a falling path for the debt-to-GDP ratio in the medium term than it has been for any of his predecessors since the OBR was established in 2010.

This is due to the combination of subdued medium term growth prospects, a stock of debt that has been pushed to a 60-year high and interest rates on that higher stock of debt, which have tripled over the past year to their highest level in over a decade.

The OBR concludes that lower energy prices and inflation – compared to recent spikes - will alleviate some financial pressure on households, businesses, and government. This will mean a shorter, shallower economic downturn this year – and avoiding a technical recession. However, persistent supply-side challenges will continue and growth will still be low.

The measures announced by Jeremy Hunt won't do much to tackle the underlying problems of low investment, stagnant living standards, public service constraints and high taxes.

Any improvement in borrowing has been off-set by nominal GDP growth and a general deterioration in the fiscal situation. However, the Budget has succeeded in the Chancellor's main objective. It steadies the ship and restores some credibility in international financial markets following the stormy waters of the previous mini Budget which rocked the Government and led to the tumultuous resignation of both the Chancellor (Kwasi Kwarteng) and the Prime Minister (Liz Truss). With a general election expected next Summer, the question remains, however, will it be enough to turn the tide in favour of Rishi Sunak?

The Spring Budget 2023 is available in full here and the Office for Budget Responsibility (OBR) economic and fiscal outlook can be accessed here. The supplementary OBR charts and tables can be found here.