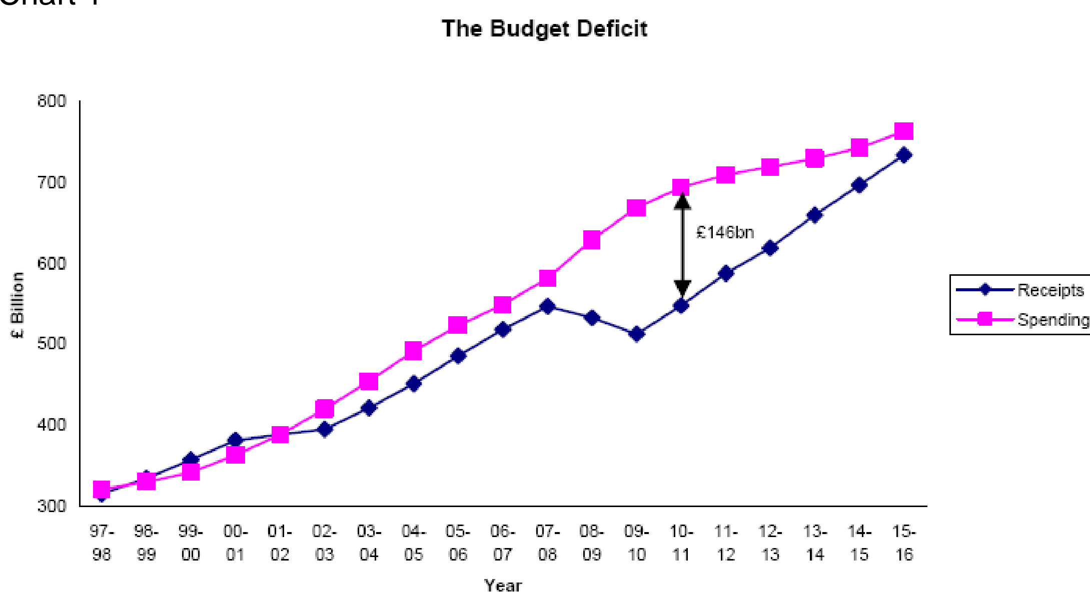
National Economic Outlook

1. The Council's financial and service planning takes place within the context of the national economic and public expenditure plans. This part of the proposals explores that context and identifies the broad national assumptions within which the proposed budget and MTFP 2012-2017 have been framed.
2. The Government has made it clear that one of its major priorities is to tackle and eliminate the national budget deficit. The Chancellor of the Exchequer outlined the Government's plans in his Emergency Budget within 6 weeks of the Coalition Government being formed. In his plan he outlined that the deficit would have to be found 80% from spending cuts and 20% from tax rises. Chart 1 below shows how it was envisaged the deficit would be eliminated through slowing the growth in public spending and increasing tax yield (mainly arising from the recovery from recession).

Chart 1



3. The Chancellor made some minor changes to the forecast deficit in his 2011 Budget announced on 23 March but has made some more significant revisions in his Autumn Statement of 29 November. In particular the forecasts for economic growth have been significantly reduced as recovery from the recession has been much slower than earlier predictions and the Gross Domestic Product (GDP) is still well below its 2008 pre recession peak. The Autumn Statement predicts it to grow by just 0.7% in 2012.
4. The low growth forecasts mean that tax receipts will be less than previously planned and as a consequence the budget deficit will not be cleared by the end of the current Parliament. The Chancellor has stuck with the spending plans announced in Spending Review 2010 (SR2010) and consequently borrowing will be higher than previously planned (although the cost of borrowing will be lower due to lower interest rates which means the cost of financing the additional borrowing will not make the deficit worse).
5. The Government has set a target of 2% for the underlying rate of inflation as measured by the Consumer Price Index (CPI). The annual rate of inflation has been running much higher than this throughout 2011. This has been ascribed to a number of factors including the impact of the VAT increase in January 2011 and volatility in commodity prices. Inflation is predicted to fall during 2012 (the impact of VAT increase will cease to be a factor after January 2012) and

the Bank of England (BoE) is expecting to reach the Government's target rate of inflation by late 2012.

6. CPI in the year to September 2011 showed an increase of 5.2% (up 0.7 percentage points on August), RPI was 5.6% (up 0.4 percentage points on August). The September indices are important as they are used to up-rate benefits, tax credits and pensions. From 2012 CPI will also be used to up-rate tax and national insurance thresholds. The December indices show a slight reduction to 4.2% (CPI) and 4.8% (RPI) due to lower fuel & clothing prices.

7. Table 1 shows the main economic indicators included in the Chancellor's statements based on the recommendations from the independent Office for Budget Responsibility (OBR).

Table 1

	2009	2010	2011	2012	2013	2014	2015
Growth % (GDP)							
Emergency Budget June 2010	-4.9	1.2	2.3	2.8	2.9	2.7	2.7
Budget March 2011	-4.9	1.3	1.7	2.5	2.9	2.9	2.8
Autumn Statement Nov 2011		1.8	0.9	0.7	2.1	2.7	3.0
Inflation % (CPI)							
Emergency Budget June 2010	2.1	2.7	2.4	1.9	2	2	2
Budget March 2011	2.2	3.3	4.2	2.5	2	2	2
Autumn Statement Nov 2011		3.3	4.5	2.7	2.1	2	2
Net Borrowing (£bn)							
Emergency Budget June 2010	154.7	149.1	116	89	60	37	20
Budget March 2011	156.4	145.9	122	101	70	46	29
Autumn Statement Nov 2011		137.1	127	120	100	79	53

8. The BoE is responsible for monetary and financial stability in the UK. The main tool at its disposal is to control the price of money through setting interest rates via the BoE base rate. The BoE responded to the recession with successive interest rate cuts in 2008 and 2009 and by March 2009 it was down to 0.5% where it has remained ever since. Many economic analysts are predicting that the rate will have to stay at this historic low for some time until the recovery is well established and growth levels are sustainable. It is feasible the BoE may have to consider further quantitative easing if growth continues to remain weak.

9. Good economic performance is essential if the Government is to meet its deficit reduction plan. This was based on a combination of recovering the overall tax yield following its decline during the recession and reducing public expenditure as a proportion of the nation's overall GDP. In reducing public spending the expectation was that the private sector would take up the extra capacity so there would not be an overall reduction in GDP. The sluggish recovery has delayed the deficit reduction plan and the government is now not expecting to meet its original target of eliminating the structural budget deficit by 2015/16.