

The OBR: almost one year old

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The evolution of the OBR to date

- Phase One
 - OBR proposed by opposition Conservative Party pre 2010 election
 - Set up in interim form by Conservative/Liberal coalition post election
 - Produced forecasts before and alongside ‘emergency’ June Budget
 - Labour Party did not oppose, but some controversy re independence
- Phase Two
 - Permanent ‘Budget Responsibility Committee’ appointed in autumn
 - Permanent staff identified, but still Treasury employees
 - Autumn forecast published, with Finance Minister responding
 - Moved out of Treasury building
- Phase Three
 - Statutory ‘non departmental public body’ since 4 April 2011
 - Dedicated staff and fixed multi-year budget

Structure of the OBR

- Formal responsibility for outputs and activity of the OBR resides with three-person 'Budget Responsibility Committee'
- Appointed (and potentially sacked) by Finance Minister, but with House of Commons Treasury Select Committee having a veto
- Current members: one think-tanker/journalist, one academic economist and one former Treasury fiscal forecaster
- Small staff of 15 civil servants. Free to hire from outside
- Annual budget of £1.75m/\$2.9m/€1.98m fixed for 4 years
- Smaller/cheaper end of international spectrum.

Role of the OBR

- “to examine and report on the sustainability of the public finances”
- In practice, to:
 - Produce the five-year Budget and autumn forecasts for the economy and public finances for which the Finance Minister used to be responsible
 - Assess on the basis of those forecasts whether the Government is on course to achieve the fiscal targets it has set itself
 - Scrutinise the Treasury’s costing of Budget tax and spending measures, saying if we agree, disagree or were given too little information to judge
 - Assess the long-term sustainability of the public finances and the health of the public sector balance sheet
- We do not:
 - Comment on the merits of specific tax or spending measures
 - Tell the government what fiscal targets to pursue
 - Assess alternative policy paths and measures
 - Give general economic policy advice

Rationale for creation of OBR

- Big literature on rationale for fiscal councils, but specifically for UK:
 - Credibility of fiscal management undermined pre-crisis by over-optimistic public finance forecasts and ‘moving the goalposts’
 - Independent analysts said forecasts overoptimistic, but government could always say it had better information on spending and revenues
 - Outsourcing official forecast addresses informational asymmetry in a way that replicating IFS-style ex ante and ex post scrutiny would not
 - But requirement to produce post-measures forecast on Budget day requires close working with HM Revenue & Customs, Department for Work and Pensions, HM Treasury and many others in government
 - Relationship with government makes transparency essential

Transparency key to credibility

- Transparency about process
 - Website and publications detail interactions with government
 - Contacts with ministers and advisers logged and published
 - Working agreements with key government departments published
- Transparency about analysis
 - Much more diagnostic material in forecast documents
 - Many more variables/assumptions published
 - More methodological material made available
 - More data on forecasts available on request
 - Clearer presentation of public finance statistics
 - Much more information on policy costing judgements

Macro-economic forecasting: why?

- OBR has no real advantage over other macro forecasters
- Inevitable forecasting errors pose risk to credibility
- But we need a disaggregated five-year forecast for fiscal forecast
- Bank of England publishes forecasts for 2 variables over 3 years
- No obvious independent or aggregate alternative

- So we do have to do a macro forecast, but emphasise uncertainty:
 - Fan charts based on past forecast errors
 - Sensitivity analysis e.g. output gap, growth rate, bond yields
 - Scenarios e.g. stubborn inflation, less rebalancing, weak euro
- But still lots of public focus on short-term forecasts

- Public debate not whether we will need additional fiscal tightening to meet targets, but whether planned tightening will kill the recovery

Some issues for the future

- How can we get the most out of our long-term sustainability analysis?
- What happens when we bring the Finance Minister bad news?
- Will we eventually be asked to look at alternative policies?
- Will parliament help our mission or hinder it?
- How vulnerable is the institution to inevitable forecasting errors?