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?