Reactions to Mr Osborne's Autumn Statement

Today, Chancellor George Osborne set out the Conservative Government's fiscal plans for the current Parliament and beyond. Although it slightly eases the speed and scope of the spending reductions from the previous July estimates, it still envisages an overall budget surplus of over £10 billion by the last year of this Parliament, 2019/20.

We give below the first reactions to the Chancellor's speech from four members of the network Economists for Rational Economic Policies (EREP) – Professor John Weeks, Dr Jo Michell, Ann Pettifor, and Jeremy Smith. Without giving away too many state secrets, they are less than impressed by the Chancellor's economic choices…

Mr Osborne spins his miserable record

Professor John Weeks, Economist, SOAS, University of London

The Chancellor's performance leaves me with three strong impressions. First, yet again he pledges to turn the fiscal balance positive by 2020. This time the pledge comes on the heels of a fiscal year when he borrowed £57 billion more than he had promised in May 2010; and achieving it requires an optimistic growth projection well above what the economy experienced under his watch. Second, according to government statistics his much trailed plan to build 400,000 new "affordable" houses by 2020 calculates to an annual increase of 0.3%, below the 0.6% rate of growth of new households.

Third, despite Osborne's miserable record – overseeing the slowest recovery on record and taking the net debt of the government from 63% of GDP in May 2010 to 81% this year – the media commentary goes after not him but the Shadow Chancellor for a poor budget performance. When Ed Miliband and John Major proposed major reform of media ownership they sure were on to something.

A gambler's implausible U-turn

Dr Jo Michell, University of the West of England, Senior Lecturer of Economics

This is a U-turn budget from the Chancellor. He has capitulated to Labour's demands and abandoned his tax credits policy. He has also cancelled all cuts to the police and stayed the axe across a range of other government departments. And yet, despite committing to a reduction in austerity totalling more than £20bn over the next parliament, the Office for Budget Responsibility (OBR) continues to project a budget surplus by 2020. How is this possible?

The answer is that the OBR has changed the model it uses to forecast tax revenues. The result is that they now predict around £27bn in additional tax revenues over the coming parliament. Past OBR predictions have not stood the test of time. In 2010, the OBR predicted that the deficit would have been eliminated by 2015 - last month, the deficit was the highest for the time of year since 2009. Borrowing this year will be around £75bn: in today's release the OBR revised this year's projected deficit *up* by around £5bn. On his own clearly-defined terms- he pledged to eliminate the deficit by 2015 - Osborne's strategy has failed.

The assumptions underlying the OBR's projections are so optimistic as to be implausible. It is assumed that growth will remain constant at around 2.5% per annum. Corporate spending and investment will pick up. The current account deficit will narrow substantially. Even taking all this into account, the OBR projections still require a deficit in the household sector greater than that in the period preceding the 2008 crisis. Any deviation from these projections will see the deficit widening and the debt-to-GDP ratio rising.

Osborne is gambling that this doesn't matter to the electorate. He got away with it in 2015. He may well get away with it again.

Is OBR's optimism misplaced?

Ann Pettifor, Director of PRIME Economics

Has George Osborne stopped beating up the economy? Certainly many are nervously relieved at having evaded the big stick he waved earlier. Others have noted that he was helped in his more benevolent approach by optimistic forecasts from the Office of Budget Responsibility (OBR).

Despite this apparent benevolence, the Chancellor still plans to cut public spending and increase taxes. The OBR forecasts that "fiscal consolidation (will) continue to depress the level of GDP, while acting as less of a drag on growth over the past four years." (OBR)

However even this bit of cheer is predicated on the global economy expanding, and inflation rising. While we can speculate that the additional stimulus applied to the private property sector may cause asset prices to rise (if house builders are confident of selling new properties at a profit, and do build) the fall in CPI has far more to do with weak domestic and global demand.

The OBR would have us believe that falls in consumer prices mainly reflect "falls in commodity prices". But falling commodity prices reflect weak *global* demand or spare capacity, and take the form of gluts and rises in inventories.

These have intensified deflationary pressures globally, but also in the euro area. Into this depressed world where economic contraction or 'austerity' is widespread, the OBR expects "UK export markets to grow by 4.1% in 2015" – higher than their July forecast. This seems somewhat optimistic.

While the OBR recognizes the UK household sector as the largest source of income and spending in the UK economy, it also expects households to save, and deleverage debt to 163% of disposable income.

This process will surely depress consumption, yet household debt will still be amongst the highest levels in the world (and because of deflation will rise in real terms) while *real* rates of interest on that debt are expected to rise.

And all of the OBR's optimism is predicated on global deflationary pressures easing. As the experience of the steel industry has shown, deflationary pressures can close down whole industries and their related sectors, raising unemployment and drastically depressing affected household income and spending. Steel will not be the only industry to be damaged by falling prices. More dominoes are due to fall.

The reasons are straightforward: the global financial crisis has not ended. On the contrary having moved from the core – the UK and US– in 2007-9, the crisis then transferred to the Eurozone, where it is ongoing. Emerging markets centred on China are now at the epicenter of the *third phase* of this apparently unending crisis. The ending of monetary stimulus in the US and fiscal contraction in important western economies has weakened demand globally, and led to a build-up of gluts in emerging markets and consequent falls in commodity prices.

At the same time there is no sign that the policies that inform the dominant debt-deflationary economic model in the UK and in most of the OECD economies - are changing.

It is therefore unlikely that the British economy will be insulated from a global crisis that this Chancellor's fiscal consolidation has made worse. He now intends, without any real changes to his economic model, to make Britain's contribution to weakening global demand less bad.

Osborne's Commedia dell'Arte e dell'Austerità

Jeremy Smith, Co-director of PRIME Economics

What we saw from George Osborne today in his Autumn Statement speech was not economics, not really politics…but comedy mixed up with tragedy – the stuff of the Commedia dell'arte.

But the most important "actors" in today's performance were off-stage – the Office for National Statistics and the Office for Budget Responsibility. And key to the production is this sentence in the OBR's Economic and Fiscal Outlook:

"Since our July forecast, the ONS has published the 2015 Blue Book."

Not only has the OBR decided that Housing Association debt counts as public debt (so changing the debt figures), but they have also incorporated significant changes by the ONS to the GDP numbers going back to the financial crisis, and which (per OBR) "revised up cumulative GDP growth since the low point of the late 2000s recession from 11.2 to 12.1 per cent."

By starting from a “better” GDP position, though nothing has changed in the real world (or economy), and by relaxing some of its future years assumptions, the OBR has opened the door to the government slightly softening its cuts, while still reaching its goal of an estimated £10 billion budget surplus in 2019/20.

For though the surplus is given in pounds, almost all the other relevant statistics on which the “deficit reduction” game is played depend on percentages of GDP.

So while the OBR keeps its 2.4% growth estimate for this year, next year it raises its estimate from 2.3% to 2.4%, and the following year from 2.4% to 2.5%.

The rationale for increasing GDP in 2016/17 is nicely ironic, given that the OBR is generally warning of increasing global economic headwinds:

“In 2016, that mainly reflects the Government’s decision to ease the pace of fiscal tightening”.

Yes, the OBR confirms the “Keynesian” multiplier effect!

The other important factor is the assumption that government income (i.e. largely taxes) will form a larger share of GDP than foreseen back in July.

On the spending side, Total Managed Expenditure(TME) – which comprises all public spending, revenue and capital – also rises (from the July estimates) as a percentage of GDP, from 38.7% to 39.1% in 2016/17, by 0.3% the following year, then by 0.2%.

Public Sector Net Borrowing as a percentage of GDP then follows this slower spending-cuts path, with the July estimate in brackets:

2015/16 - 3.9% (3.7%); 2016/17 - 2.5% (2.2%); 2017/18 - 1.2% (1.2%); 2018/19 - 0.2% (0.3%); 2019/20 - +0.5% (+0.4%)

All of these shifting numbers and percentages lead to one solid conclusion. The Chancellor – any Chancellor – has plenty of room for fiscal manoeuvre, provided that the general direction of the economy is understood. As I sought to show recently, there is no economic reason whatsoever for further cuts.

The whole comedy and tragedy is driven by one and only one concern – that our hero finally, having slain every dragon and serpent in his path, gets the Holy Grail. A Wholly unnecessary Grail that neither helps our public finances nor enhances our economic security.