Statistical Factsheet 5

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Through rose-tinted glasses: the recent history of Treasury forecasts

- In May 2010, the new Chancellor George Osborne set up the independent Office for Budget Responsibility. Its role is to give independent assessments of both the public finances and wider economic indicators.

- But why was this necessary? For the past ten years there has been a suspicion that the Treasury's forecasting model tends to be 'over-optimistic' about the growth prospects of the economy.

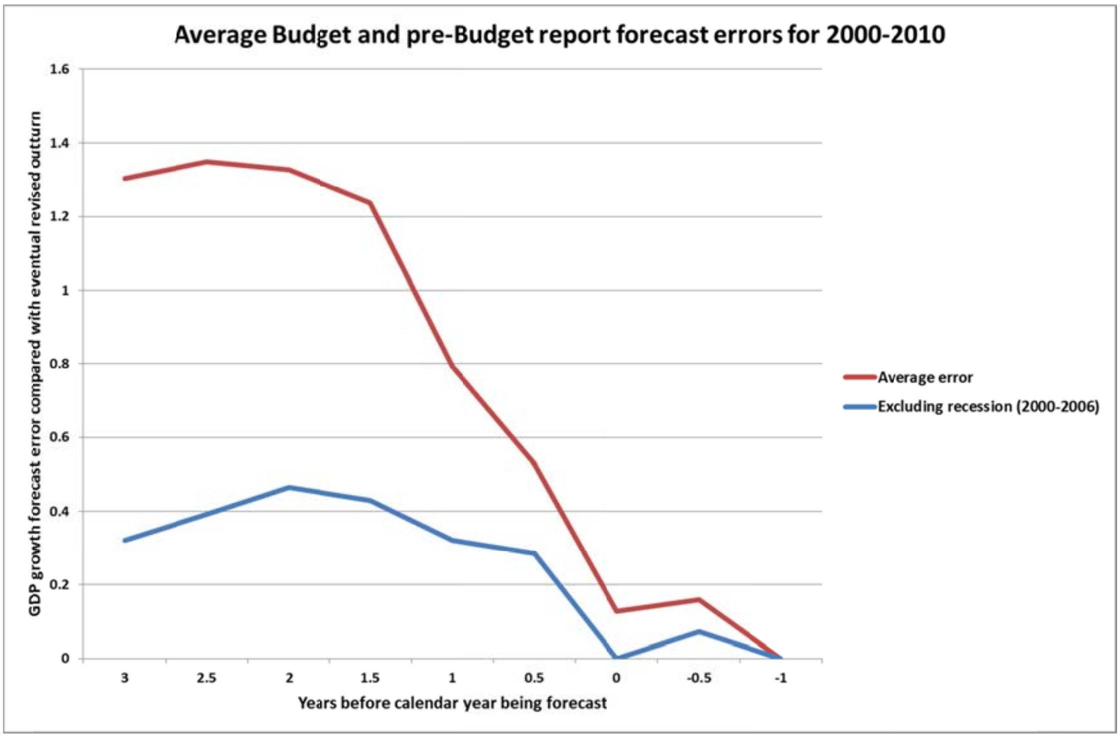
- Budget and pre-Budget reports going back to November 1997 allow us to compare forecasts of annual GDP growth with eventual revised outturn (as presented in later Budget/pre-Budget reports).

- Our calculations show that Treasury forecasts of GDP growth three years ahead were over-optimistic on average by 1.3% for the period from 2000 and 2010; two years ahead were over-optimistic by an average of 1.3%; and forecasts were still over-optimistic by 0.75% just one year before the outturn.

- Even stripping out the recession post-2007, and focusing solely on the 'good' years of 2000 to 2006, an upward bias persists. Forecasts tended to be on average 0.3% above revised outturn three years ahead, 0.5% two years ahead and 0.3% one year ahead.

- The forecasts have been particularly poor for 2007-2010. Because of the recession, the average forecast three years ahead was on average 3% too optimistic for this period, 2.8% too optimistic two years ahead and 1.6% too optimistic one year ahead.

- At best this evidence shows the difficulty of accurate macroeconomic growth forecasting. At worst, it provides strong justification for setting up the independent Office for Budget Responsibility.



Sources: HM Treasury Budget Report and Pre-Budget Reports, 1997 onwards