

The Scottish Budget 2018/19, introduced in draft form in December last year and finalised in February, was informed by revenue forecasts made by the Scottish Fiscal Commission. Three of these revenue forecasts were particularly relevant: those for Scottish income tax; Land and Buildings Transactions Tax (LBTT); and Scottish Landfill Tax.

Forecasts are inevitably subject to change as new information comes to light. There was always a likelihood therefore that the Scottish Government might end up having somewhat more, or somewhat less, resources available to it in 2018/19 than it thought when the budget was set.

Today the SFC has published updated forecasts for the 2018/19 financial year and beyond. How do these change the outlook for the Scottish Government's resource budget in 2018/19?

Firstly, the forecast for income tax revenues in Scotland has been revised down by £208m (1.7%).

Does this mean that the Scottish Government has £208m less to spend in 2018/19 than it thought a few months ago? Not necessarily! Under Scotland's Fiscal Framework, what is as important as the revenues raised from each tax is the deduction that is made from the block grant for each tax - the so-called 'Block Grant Adjustment'. The BGAs are designed to represent the revenues foregone by the UK Government as a result of transferring the tax to Scotland - and they are linked to the growth rate of revenues in the 'equivalent' taxes in the rest of the UK.

This means that a forecast for lower income tax revenues in Scotland could be offset by a lower forecast for income tax revenues in rUK (which would reduce the income tax BGA). But if the reduced forecast for Scottish income tax goes alongside an increase in the rUK forecast, the Scottish budget could actually be worse off than implied by the SFC's forecast alone. In other words, revisions to Scottish revenues have to be compared alongside revisions to the BGAs.

When the OBR updated its UK forecasts in March this year (alongside the UK Government's Spring Statement), the income tax forecast was actually revised up by £181m.

So in fact, the outlook for the Scottish Budget has worsened in two ways since a few months ago. Not only has the forecast for income tax been revised down by £208m, but the BGA has been revised up by £181m. The net effect of these two revisions on their own is that the Budget is £389m worse off than a few months ago.

There is however an important caveat. The Scottish Government does not have to adjust its 2018/19 spending plans immediately on the basis of these latest forecasts. The forecasts that the SFC and OBR made at the end of 2017 are the ones that 'count', until outturn data is available. The Scottish Government can hope therefore that the outturn data (which will not be available in fully audited form until 2020) looks more like the December forecast than these most recent forecasts.

But at the same time, the Government will no doubt be beginning to plan how it might deal with a revenue shortfall if it emerges. This may include use of revenue borrowing powers (which are normally capped at £300m for forecast error), and the Scotland Reserve (effectively a 'rainy day fund' which is currently in credit to the tune of about £74m).

In relation to LBTT and Landfill Tax there is somewhat better news. The forecasts for both LBTT and Landfill Tax have been revised up. The forecast for LBTT is up £26m (4.4%), whilst the Landfill Tax forecast is up £8m (7.6%). At the same time, whilst the latest BGA for Landfill Tax is £12m higher than it was at the time the Scottish Budget was set, the BGA for LBTT has been revised down by £12m.

In net terms therefore, taking both revenues and BGAs into consideration, the outlook for the Scottish budget has improved by around £38m in relation to LBTT, worsened by about £4m in relation to Landfill Tax, and worsened in relation to income tax by around £389m.

The table below summarises the change in the outlook for the 2018/19 budget. Remember however, the May 2018 figures represent the latest outlook, but they do not imply an immediate shift in the Government's spending power.

Table 1: Forecast changes, £m

		Budget 2018/19	Fiscal Outlook May 2018	Change
Income tax	Revenue	12177	11969	-208
	BGA	11749	11930	181
	Net	428	39	-389
LBTT	Revenue	588	614	26
	BGA	600	588	-12
	Net	-12	26	38

Implications of today's forecast revisions for the 2018/19 budget

	Revenue	106	114	8
Landfill Tax	BGA	94	106	12
	Net	12	8	-4
	Revenue	12871	12697	-174
Total	BGA	12443	12624	181
	Net	428	73	-355

This pattern of revisions is effectively repeated in future years (i.e. the outlook for the Scottish budget in 2019/20 is now around £400m lower than was the case in February).

Why have the income tax forecasts for Scotland been revised down so much in a relatively short space of time? And what are the implications for the Government's wider spending priorities? We will consider these questions in subsequent blogs.