This blog post contains the policy context chapter of our economic commentary, published today. The latest economic commentary can be found here.

Budget 2020/21 will be the fourth of five to be set in this parliament. Normally of course it would have been published by now – the Scottish Government initially planned to publish it on 12 December – and the process of scrutiny and debate on the proposals contained within it would have begun.

It was inevitable that the announcement of a UK General Election on 12 December resulted in the postponement of the Scottish budget. The outlook for the Scottish budget – and the viability and outcomes of tax and spending policies – is heavily dependent on UK Government policy decisions.

A Scottish budget published in advance of knowing the complexion of the UK Government would have had to be underpinned by a range of caveats and uncertainties, and could have been subject to substantial revision once the UK Government's plans became known with greater certainty.

The fact that the General Election result last week was so decisive has in a blink lifted much of the uncertainty that it existed, at least in the short run (i.e. for 2020/21).

The departmental spending plans of the Conservative Government for 2020/21 are unlikely to differ substantially from those set out in September's Spending Round (and reiterated in the Conservative manifesto). There may be a few extra spending announcements here or there, but the UK Chancellor has little scope to announce anything significant given his stated fiscal rule and his party's commitment to avoid tax increases.

In principle the Chancellor could be dealt a helping hand by the OBR if it revises up its forecasts for UK economic growth. But the prospect of this seem unlikely in the context of economic data published since the OBR's last forecasts in March this year (the March forecasts were made on the assumption that the UK exited the EU on terms not dissimilar from those negotiated by Mr. Johnson).

So, on the assumption that the UK Government's spending plans do not differ materially from those set out in September, the implication is that the Scottish resource block grant will increase by around £1.1bn, or just over 2% in real terms in 2020/21.

However, the resources available to the Scottish Government may increase somewhat less than this for two reasons – one of which we have certainty on, the other is more uncertain.

- First, the block grant will be reduced by £200m to reflect forecast error in relation to the income tax forecast for the 2017/18 budget. Long lags between budget forecasts and income tax reconciliations are an unfortunate side effect of the new fiscal powers.
- Second, it seems likely that the SFC's forecasts for Scottish income tax revenue growth in 2020/21 may point to somewhat less revenue being raised through this channel than in 2019/20. This is by no means a given, and it will depend on a variety of factors, including how the SFC choose to interpret recent (relatively positive) economic data for Scotland in the context of longer term trends.

A central assumption therefore is that the Scottish Government's resource budget will rise by around 2% in real terms, assuming no major tax policy changes. This would take the Scottish budget to around 4% higher in real terms than in 2016/17.

Whilst this is not a huge increase in a historic context (and the budget would remain some 3% lower than in the pre-austerity peak of 2010/11), it represents a marked improvement on the outlook Mr. Mackay faced at the end of 2016. Then, the outlook was for real terms decline in the block grant of over 3% to 2019/20.

On the spending side, we can expect a continuation of the trends in previous budgets of this parliament. Health spending is likely to increase 3 or 4 per cent in real terms.

Alongside (much smaller) commitments on police, education and childcare, expect a further debate about the constraints faced by local government. In this context it will be interesting to see how much further the debate on local taxation gets.

Local authorities do have the power to set a 'workplace parking levy' in their areas, and the Programme for Government included an intention to create a discretionary power to enable councils to introduce a tourist visitor levy. And as part of last year's budget, the government committed to convene cross-party talks on replacing the current council tax – although we have of course been here several times before.

But the pace of reform on local government finance has been slow. This no doubt explains, in part why many in Parliament are supporting the decision to devolve business rate setting to local authorities. There are clearly risks with such a move, and it should be part of a much wider discussion about the future of local government funding more generally rather than a policy in isolation.

As well as local government, some other spending areas have also been consistent losers so far this parliament, including universities, environment agencies, prisons, and some other elements of the justice portfolio. Thus far there has been relatively little acknowledgement of this, and it will be interesting to see whether there becomes a point where these trends attract greater attention.

The big change happening to the Scottish budget in 2020/21 is the transfer of financial responsibility for a further five of the eleven social security payments that are being devolved following the recommendations of the Smith Commission. This will mean that the Scottish Government has assumed financial responsibility for 9 of the 11 payments being devolved by April 2020.

The transfer of financial responsibility exposes the Scottish budget to the risk that spending on the payments transferred is higher than the increase to the Scottish block grant. This is unlikely to happen in a significant way in the short run, not least because the Scottish Government will only be able to roll out new Scottish specific policy gradually over the next few years.

But the risks will grow in coming budgets. Spending on the devolved payments could increase more rapidly than the uplift to the block grant if the eligible population (largely consisting of older people) grows more quickly in Scotland than in the rest of the UK.

But it could also occur if the Scottish Government sets a policy that is more generous than the equivalent policy in rUK. The indications are that this is the direction of travel the government intends to take.

These are perfectly legitimate policy choices, and it is clearly the intention of devolution that it enables policy to evolve differently in Scotland. But higher spending on the social security payments being devolved will mean reduced spending on other areas or increases in tax.

What about the outlook for capital spending?

Last year the Scottish Government announced what appeared at the time to be an ambitious aspiration to increase capital investment in Scotland by £1.5bn by 2025.

In their Manifesto, the Conservatives said they will allow net investment to rise to 3% of GDP (from just over 2% currently). This would result in an additional £1.7bn (one third) in real terms flowing to the Scottish Government to fund capital investment in Scotland by 2023/24. On this basis, the Scottish Government's capital investment pledge could be met – and then some – without it needing to use its capital borrowing powers or more 'innovative' forms of investment.

Of course we still do not yet know when the Scottish budget will be.

The UK budget is expected to be published in February, after the UK has officially left the EU at the end of January. An announcement on a specific date can be expected soon.

If the UK budget is published in early February, the Scottish budget will probably follow 2-3 weeks later, following which there will be an extremely short period of parliamentary debate, a truncated legislative process, and an expedited process of Royal Assent for the Budget Bill (and related legislation, including the Scottish Rate Resolution on income tax and the Local Government Finance Order).

If the UK budget is published later in February, there may be no option other than to prepare the Scottish budget concurrently, publishing it at around the same time. If the UK budget contained any particular surprises in terms of spending lines or tax policy, the Scottish Government may end up having to amend its budget mid-way through a scrutiny or legislative process that had already begun.

Beyond the 2020/21 budget itself, the UK Government is likely to aim to publish a multi-year spending review towards the summer, enabling the Scottish Government to follow suit with its own spending review, possibly in summer.

The hope of many in the public sector will be that the Scottish Government finally gets around to setting a multi-year spending framework as opposed to the more opportunistic decision of recent times to set one-year budgets.

In the context of the near future outlook however, all eyes will be on the publication of the 2018/19 Scottish income tax outturn data in July 2020. The latest forecasts indicate that this outturn figure might be 'bad' for Scotland for two reasons:

- First, because it will indicate (if latest forecasts are to be believed) that the Scottish income tax base grew relatively weakly in 2018/19, offsetting any hoped-for boost from the income tax policy introduced in Scotland that year.
- Second, because this weaker performance wasn't forecast at the time the 2018/19 budget was set, it effectively means the Scottish budget has not yet incurred the costs of this weaker tax revenue growth. A reconciliation will apply to the 2021/22 budget to reflect the extent of this forecast error.

The big question remains how large this adjustment will need to be, which is why the outturn data is so important. Indications are that it could be as high as £600m. If this is realised, it will create some interesting debates in the lead-up to the final budget of this parliament.

More generally, the prospect of a Brexit-focussed, Boris Johnson-led Conservative government at Westminster with SNP dominance in Scotland means that constitutional questions will remain dominant in the political debate.

And as well as its principle demand for a further independence referendum, its worth remembering that the SNP manifesto also called for devolution of a number of further economic and fiscal powers.

These included the devolution of powers over migration, devolution of National Insurance Contributions and devolution of aspects of employment law (including the minimum wage).

Together with an ongoing debate over what should replace various EU funds post-Brexit, it is not unlikely that we will spend much of the year debating what fiscal and economic powers the Scottish Government should be able to exercise in future, and relatively less on how the existing powers are being used today.