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**REPORT FROM THE COMMISSION**

**United Kingdom**

**Report prepared in accordance with Article 104(3) of the Treaty**

{SEC(2008) 2016}

# REPORT FROM THE COMMISSION

## United Kingdom

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#### 1. INTRODUCTION

This report assesses recent and current budgetary developments in the United Kingdom and reviews the short- and medium-term prospects in the light of overall economic conditions and policy action taken by the government. It is prepared according to Article 104(3) of the Treaty and follows the United Kingdom's announcement of a *planned* deficit exceeding the reference value.

Article 104 of the Treaty lays down an excessive deficit procedure (EDP). This procedure is further specified in Council Regulation (EC) No 1467/97 “on speeding up and clarifying the implementation of the excessive deficit procedure”<sup>1</sup>, which is part of the Stability and Growth Pact. While the provisions above apply to the UK in the same manner as to other countries not participating in the euro area, it should be recalled that under Article 5 of the Protocol on certain provisions relating to the United Kingdom of Great Britain and Northern Ireland, the obligation under Article 104(1) of the Treaty to avoid excessive general government deficits does not apply to the United Kingdom unless it moves to the third stage of EMU. Instead, as long as it is in the second stage of EMU, the UK is committed under Article 116(4) of the Treaty to “endeavour to avoid excessive deficits”.

According to Article 104(2) of the Treaty, the Commission has to monitor compliance with budgetary discipline on the basis of two criteria, namely: (a) whether the ratio of the planned or actual government deficit to gross domestic product (GDP) exceeds the reference value of 3% (unless either the ratio has declined substantially and continuously and reached a level that comes close to the reference value; or, alternatively, the excess over the reference value is only exceptional and temporary and the ratio remains close to the reference value); and (b) whether the ratio of government debt to GDP exceeds the reference value of 60% (unless the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace).

Article 104(3) stipulates that, if a Member State does not fulfil the requirements under one or both of these criteria, the Commission has to prepare a report. The report also has to “take into account whether the government deficit exceeds government investment expenditure and take into account all other relevant factors, including the medium-term economic and budgetary position of the Member State”.

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<sup>1</sup> OJ L 209, 2.8.1997, p. 6. Regulation as amended by Regulation (EC) No 1056/2005 (OJ L 174, 7.7.2005, p. 5). The report also takes into account the “Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes”, endorsed by the ECOFIN Council of 11 October 2005, available at [http://ec.europa.eu/economy\\_finance/about/activities/sgp/main\\_en.htm](http://ec.europa.eu/economy_finance/about/activities/sgp/main_en.htm).

The preceding EDP in respect of the United Kingdom (its third such procedure<sup>2</sup>) was abrogated in October 2007. This was initiated in September 2005 with the Commission's adoption of a report under Article 104(3) following the August 2005 EDP notification which reported a general government deficit ratio of 3.2% in the financial year 2004/05<sup>3</sup>. In January 2006, the Council decided, on a recommendation from the Commission, that the United Kingdom was in excessive deficit according to Article 104(6)<sup>4</sup>. At the same time, and also based on a Commission recommendation, the Council addressed recommendations under Article 104.7 to the UK with a view to bringing the situation of an excessive government deficit to an end by 2006/07 at the latest. On 12 September 2007, the Commission adopted a recommendation for a Council decision abrogating the procedure. On 9 October 2007, the Council decided to abrogate the EDP according to Article 104.12 of the Treaty.

According to the EDP data notified by the UK authorities in March 2008<sup>5</sup>, the general government deficit in the United Kingdom was planned to reach 3.2% of GDP in 2008/09, thus exceeding the 3% of GDP reference value, while general government gross debt would be 43.0% of GDP<sup>6</sup>, below the 60% of GDP reference value but on a rising trend; these ratios are identical to those published in the United Kingdom's March 2008 budget. A subsequent policy announcement on 13 May reducing personal income tax in 2008/09, financed by additional borrowing (see Section 2) results in higher planned deficit and debt ratios than those in the notification.

**Table 1: General government deficit and debt <sup>a</sup>**

	2004/05	2005/06	2006/07	2007/08	2008/09		2009/10	
					COM	2008 budget <sup>b</sup>	COM	2008 budget <sup>b</sup>
General government balance	3.5	3.1	2.6	2.9	3.3	3.2	3.3	2.8
General government gross debt	39.7	41.7	42.5	43.2	46.2	45.2	47.5	46.1

Note:

<sup>a</sup> In percent of GDP.

<sup>b</sup> The projections notified in March 2008 are identical to those published in the 2008 budget.

Source: Eurostat, Commission services' spring 2008 forecasts and 2008 Budget

The figure for the 2008/09 deficit in the notification provides *prima facie* evidence of a planned excessive deficit in the United Kingdom in the sense of the Treaty and the Stability and Growth Pact, while the more recent policy announcement is additional evidence. The Commission has therefore decided to initiate the excessive deficit procedure for the United Kingdom with the adoption of this report. Section 2 of the report examines the deficit criterion and Section 3 the debt criterion. Section 4 deals with public investment and other

<sup>2</sup> The first EDP vis-à-vis the United Kingdom was abrogated in 1998. Following a deficit outturn of 3.2% of GDP in 2002/03, in April 2004 the Commission initiated a second EDP with an Article 104.3 report. Given expectations that the excessive deficit would revert to below the threshold level in the following year, the Commission and the Economic and Financial Committee then concluded that the United Kingdom could not be considered to be in an excessive deficit situation as defined in the Treaty.

<sup>3</sup> The UK financial year runs from April to March. The EDP applies to the UK on a financial year basis (annex to Regulation No 1467/97).

<sup>4</sup> All EDP-related documents for the United Kingdom can be found at the following website: [http://ec.europa.eu/economy\\_finance/netstartsearch/pdfsearch/pdf.cfm?mode=\\_m2](http://ec.europa.eu/economy_finance/netstartsearch/pdfsearch/pdf.cfm?mode=_m2)

<sup>5</sup> According to Council Regulation (EC) No 3605/93, Member States have to report to the Commission, twice a year, their planned and actual government deficit and debt levels. The most recent notification of the United Kingdom can be found at:

[http://epp.eurostat.ec.europa.eu/portal/page?\\_pageid=2373,58110711&\\_dad=portal&\\_schema=portal](http://epp.eurostat.ec.europa.eu/portal/page?_pageid=2373,58110711&_dad=portal&_schema=portal).

<sup>6</sup> Using FISIM-adjusted version of GDP.

relevant factors. The technical analysis underpinning the conclusions of the report is provided in a more detailed Commission staff working document, which is released in parallel with this report<sup>7</sup>. Both documents take into account the Commission services' spring 2008 forecasts, released on 28 April.

## 2. DEFICIT CRITERION

In 2008/09, the general government deficit was planned to reach 3.2% of GDP in the March 2008 notification.

- Although in excess of 3% of GDP, the planned deficit is close to the Treaty reference value.
- The planned excess over the 3% of GDP reference value is not exceptional. In particular:
  - i) it does not result from an unusual event in the sense of the Treaty and the Stability and Growth Pact;
  - ii) It does not result from a severe economic downturn in the sense of the Treaty and the Stability and Growth Pact. GDP growth in 2006 and 2007 was above potential, with an annual outturn of 2.9% and 3.0% respectively. For the years 2008 and 2009, the Commission services' spring 2008 forecast can be considered as an up-to-date assessment of the UK's economic prospects. This forecast projects UK growth to slow in 2008 and 2009 to annual rates below potential, due to a weakening of domestic demand driven by adverse credit conditions as a result of the turmoil in financial markets, a weaker housing market and higher inflation weakening real disposable incomes. The spring 2008 forecast is more cautious than the UK's budget forecast regarding the speed of reversion to normal credit market conditions, including for secured and unsecured household borrowing, which the spring forecast expects to last into 2009. The expected improvement in net exports is not able to fully compensate for the shortfall in domestic demand. Nevertheless, quarterly GDP growth is expected to remain positive and annual GDP growth to reach 1.7% in 2008 and 1.6% in 2009. These growth rates are on a par with the average of independent forecasts in May 2008, as compiled by the UK Treasury.<sup>8</sup> On a financial year basis, the spring forecast expects GDP growth of 1.4% in 2008/9 and 1.8% in 2009/10.
- The planned excess over the 3% of GDP reference value is not temporary in the sense of the Treaty and the Stability and Growth Pact. In 2009/10, assuming that the government will adhere to the non-cyclical primary expenditure plans that were announced in the 2008 budget, the Commission services' spring 2008 forecast had projected the deficit to remain at 3.3% of GDP, with the weak economic context feeding-through into slow revenue growth. In marked contrast, the March 2008 budget projection is of a 2009/10 deficit of 2.8% of GDP, with the government's greater optimism based on an earlier and stronger economic recovery than in the Commission services' spring forecast: growth of 1¾% in 2008/9 followed by a rebound to 2½ % in 2009/10.

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<sup>7</sup> Technical document by the Commission services accompanying the report on the United Kingdom prepared in accordance with Article 104(3) of the Treaty [ECFIN/G1/2008/REP 52966].

<sup>8</sup> HM Treasury (2008): Forecasts for the UK economy – A comparison of independent forecasts, May 2008 (<http://www.hm-treasury.gov.uk/media/0/C/200805forcomp.pdf>).

**Table 2: Macroeconomic and budgetary developments <sup>a</sup>**

	2004/05	2005/06	2006/07	2007/08	2008/09		2009/10	
					COM	2008 Budget	COM	2008 Budget
Real GDP (% change) <sup>b</sup>	3.3	1.8	2.9	3.0	1.7	2.0	1.6	2½
Potential GDP (% change) <sup>b,c</sup>	2.7	2.7	2.8	2.7	2.4	2½	2.3	2½
Output gap (% of potential GDP) <sup>b,c</sup>	0.7	-0.1	0.0	0.4	-0.3	-0.6	-1.0	-0.6
General government balance	3.5	3.1	2.6	2.9	3.3	3.2	3.3	2.8
Primary balance	-1.4	-1.0	-0.4	-0.7	-1.1	-1.2	-1.2	-0.8
One-off and other temporary measures	-	0.3	-	-	-	-	-	-
Government gross fixed capital formation	1.8	0.6	1.8	1.9	2.0	2.0	1.9	2.0
Cyclically-adjusted balance <sup>c,d</sup>	-3.7	-3.0	-2.7	-3.0	-3.1	-2.9	-2.9	-2.6
Cyclically-adjusted primary balance	-1.7	-0.9	-0.6	-0.8	-0.9	-0.9	-0.8	-0.6
Structural balance <sup>d,e</sup>	-3.7	-3.3	-2.7	-3.0	-3.1	-2.9	-2.9	-2.6
Structural primary balance	-1.7	-1.2	-0.6	-0.8	-0.9	-0.9	-0.8	-0.6

**Notes:**

<sup>a</sup> In percent of GDP unless specified otherwise.

<sup>b</sup> Data on a calendar-year basis. Numbers reported in 2004/05 column refer to the 2004 calendar year.

<sup>c</sup> Potential GDP growth, output gaps and cyclically-adjusted balances attributed to the 2008 budget are reported as recalculated by the Commission services on the basis of the information in the budget.

<sup>d</sup> The 2008 budget estimate of the cyclically-adjusted and structural balances in 2007/08 (as recalculated by the Commission services) is 2.8% of GDP.

<sup>e</sup> Cyclically-adjusted balance excluding one-off and other temporary measures.

*Source: Eurostat and Commission services' spring 2008 forecasts.*

However, the Commission's spring 2008 fiscal projections (and the 2008 budget report) predated the government's statement on the 23 April 2008 that it now envisaged elements of compensation to some of those negatively affected by the removal from April 2008 of the 10% starting rate of income tax (one of the measures announced in the March 2007 budget). An initial measure announced on 13 May 2008 is a reduction in personal income tax in 2008/09 financed by additional borrowing, which will lead to an increase in the deficit in 2008/09 by 0.2 percentage points of GDP, increasing the deficit forecast by the Commission services to 3.5% of GDP. The government announced in its statement that for future years it aims to "*continue the same level of support for those on lower incomes*"<sup>9</sup>. The announcement does not commit the government to extend to 2009/10 the fully debt-financed compensation offered in 2008/09 (thus opening the possibility of offsetting tax and expenditure measures<sup>10</sup>). It nevertheless carries a significant risk for 2009/10 of a deficit overshoot, compared with the March 2008 budget plans, with a similar impact *ceteris paribus* on the spring forecast projection.

In sum, the planned deficit is close to the 3% of GDP reference value but the planned excess over the reference value is neither exceptional nor temporary in the sense of the Treaty and the Stability and Growth Pact. This analysis suggests that the deficit criterion in the Treaty is not fulfilled.

<sup>9</sup> See paragraph 35 of the statement by the Chancellor:  
[http://www.hm-](http://www.hm-treasury.gov.uk/newsroom_and_speeches/speeches/statement/Speech_statement_130508.cfm)

<sup>10</sup> Further policy announcements are expected in the autumn 2008 Pre-Budget Report.

### 3. DEBT CRITERION

The UK's general government gross debt ratio is set to remain under the reference value of 60% of GDP within the medium term, even if projected to be on a rising trend up to 2009/2010. The spring 2008 forecast estimates that the gross debt at end-2007/08 rose to 43.2% of GDP and forecasts a further increase in the debt ratio to 46.2% of GDP by 2008/09 and 47½% by 2009/10 (see Table 1); following the 13 May announcement, prospects are for slightly higher ratios. The acceleration in the accumulation of government debt is in part due to the deterioration in the primary balance. However, in 2008/09 the forecast 3-percentage point rise in the debt ratio over the preceding year also reflects the denominator-effect from lower growth in real GDP and the GDP deflator, as well as a stock-flow adjustment of almost 1% of GDP due to the expected replacement of the Bank of England's loan to Northern Rock bank, extended progressively from September 2007, by direct government financing (see Section 4.4 below).

This analysis suggests that the debt criterion in the Treaty is fulfilled.

### 4. RELEVANT FACTORS

Article 104(3) of the Treaty provides that the Commission report “shall also take into account whether the government deficit exceeds government investment expenditure and take into account other relevant factors including the medium-term economic and budgetary position of the Member State”. These factors are further clarified in Article 2(3) of Council Regulation (EC) No 1467/97, which also specifies that “any other factors which, in the opinion of the Member State concerned, are relevant in order to comprehensively assess in qualitative terms the excess over the reference value and which the Member State has put forward to the Commission and to the Council” need to be given due consideration.

In view of the above provisions, the following four subsections consider in turn (1) the medium-term economic position; (2) the medium-term budgetary position (including public investment); (3) other factors put forward by the Member State; and (4) other factors considered relevant by the Commission.

#### *4.1. Medium-term economic position*

##### **Cyclical conditions and potential growth**

Having grown at rates slightly above potential in 2006 and 2007, the spring 2008 forecast suggests that in 2008 and 2009 the UK economy will experience a period of weak economic growth relative to potential. This moderation is largely the result of a broad-based weakening of domestic demand, although accompanied by an improvement in external demand due to the sizeable depreciation of sterling. The latter will help to correct the UK's current account deficit which reached 4.2% of GDP in 2007. With potential growth rates estimated at slightly below 2½%, expected GDP growth of 1.7% and 1.6% in 2008 and 2009 respectively will lead to a negative output gap of around 1% of GDP by the end of the forecast horizon. This output gap profile is consistent with a downturn into bad economic times in the years 2008 and 2009, but does not constitute a severe economic downturn.

##### **Recent structural reforms**

Notwithstanding a relatively strong growth performance in recent years and very flexible labour, capital and product markets, the UK still seems to face a productivity challenge. In 2006, the UK's GDP per hour worked was 4% below the euro area average. However, the UK has been catching up, with average annual growth in labour productivity over 2001-2006 of 2.1% compared to 1.0% in the euro area. Structural policy measures have focused on

improving skills, R&D and innovation, the science base, regulation, the competition regime and public services productivity, in line with the priorities put forward in the UK national reform programme (including the latest 2007 implementation report) in the context of the Lisbon strategy for growth and jobs. According to the 2007 Comprehensive Spending Review, UK science spending is expected to remain stable over the next three years at around 0.4% of GDP. If implemented fully, the long-term impact of the reform efforts on growth (and thereby the budgetary position) is likely to be positive.

#### **4.2. Medium-term budgetary position**

##### **Structural deficit and fiscal consolidation in good times**

Following the remarkable fiscal consolidation achievements during the late 1990s, the fiscal stance eased in the early 2000s, mainly on account of an explicit policy objective to raise significantly expenditure on public services. As a result, the UK general government balance moved from a surplus position in the late 1990s to a headline deficit of 3.5% of GDP in 2004/05, equivalent to a deterioration of the structural balance of 4½ percentage points of GDP<sup>11</sup> between 1999/00 and 2004/05. In 2005/06 and 2006/07, strong growth in taxes on corporate profits, boosted by higher tax intakes from the financial sector as a result of strong equity market performance and mergers and acquisition activity, contributed to an improvement in the headline and structural deficit estimates. However, the underlying budgetary situation in 2007/08 deteriorated, notwithstanding economic good times. As a result of pro-cyclical fiscal policy in 2007/08, the structural deficit in that year is estimated to have increased by ¼ percentage points, to 3% of GDP. Looking forward, the Commission services' spring 2008 forecast had projected a further weakening of the budgetary position in 2008/09, with the economic slowdown feeding through into slower revenue growth. However, the fiscal relaxation announced by government in May 2008 implies that the headline deficit is now expected to reach 3.5% of GDP, with the structural deficit ratio set to increase by ¼ percentage points. The spring 2008 forecast had estimated the structural deficit in 2009/10 at around 3% of GDP, ⅓ percentage points less than the latest estimate of the structural deficit in 2008/09. The latter in part reflects the combined effects of discretionary measures, including the higher taxes on alcohol and motor vehicles announced in the 2008 budget, and continued slower growth in government expenditure. However, the government's commitment to continue providing an unspecified level of compensation to low-income households beyond 2008/09 carries a significant risk that the reduction in the structural deficit ratio in 2009/10 could actually fall short of this.

##### **Public investment**

General government gross fixed capital formation has increased from 1.2% of GDP in 2000/01 to 1.9% in 2007/08, mirroring the government's policy of increasing public investment from the relatively low levels seen in previous years. Since 2002/03, however, the general government deficit ratio has consistently exceeded the ratio of gross fixed investment to GDP. According to the Commission services' forecasts, the general government deficit ratio will continue to exceed the gross fixed investment ratio throughout the forecast period. Between 2007/08 and 2008/09 the government investment ratio is forecast to increase by 0.1 percentage points, to 2.0% of GDP, while the headline deficit (prior to the 13 May announcement) was forecast to rise by 0.4 percentage points.

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<sup>11</sup> Estimated by the Commission services, applying the common methodology on estimating output gaps.



## **Quality of public finances**

In recent years the ratio of general government expenditure to GDP has risen by more than 5 percentage points from 39% in 1999/00 to 44% in 2006/07. In comparison, the EU average was around 47% in both 1999 and 2006. Underpinning the rise in the United Kingdom is the government's policy of increasing expenditure on public services, with a particular focus on increasing public investment from the relatively low levels seen in previous years. The 2007 Comprehensive Spending Review (CSR) – announced together with the 2007 Pre Budget Report in October 2007 – set departmental spending plans and priorities for the years 2008/09, 2009/10 and 2010/11. The spending plans over the 2007 CSR period envisage sharply lower growth in comparison with previous spending reviews. Total public spending is expected to increase by an average of 2.1% per year in real terms in the 2007 CSR period, against an average of 4.0% for the spending reviews covering the period from April 1999 to March 2008. To support the departmental spending plans and enable the release of resources for priority areas, the government has also introduced a range of initiatives within the context of the 2007 CSR to further enhance the efficiency and effectiveness of public spending, including a value for money programme and a performance management framework. It is still too early to judge whether the introduced measures will actually lead to a real improvement in the efficiency of public spending. There is a risk that some of the declared efficiency gains could represent pure cost-savings, entailing lower public service quality or output. Furthermore, the targets are intrinsically hard to evaluate.

## **Long-term sustainability of public finances**

The United Kingdom appears to be at medium risk with regard to the sustainability of public finances. The gross debt ratio, even if rising, is currently well below the 60% of GDP Treaty reference value. The long-term budgetary impact of ageing is close to the EU average, with public pension expenditure showing a somewhat more limited increase than on average in the EU, in part as a result of the fact that the UK relies relatively more on private pension arrangements than do other EU countries. The comprehensive pension system reforms adopted in 2007, addressing the concern of potentially inadequate future provision, are likely to involve a somewhat higher increase in age-related expenditure. Commission analysis based on the budgetary position in calendar year 2007 indicates that sustainable public finances are at risk, a conclusion which is aggravated when the long-term budgetary impact of an ageing population is also taken into account. Achieving high primary surpluses would contribute to reducing risks to the sustainability of public finances.

### ***4.3. Other factors put forward by the Member State***

In a letter of 20 May 2008, the authorities of the United Kingdom listed some relevant factors in accordance with Article 2(3) of Council Regulation (EC) No 1467/97. The authorities noted that public finance projections contained in Budget 2008 were based on cautious, independently audited assumptions, an approach designed to build additional contingency into the headline fiscal numbers and to protect against unexpected events. The forecasts incorporate negative impacts and downward revisions in a range of areas including tax revenues from the financial sector, and from the property market. The authorities note that the increase in the deficit projected in Budget 2008 reflects the operation of the automatic stabilisers as well as non-discretionary factors, in the short term, resulting from exceptional disruption in global financial markets. The letter notes that UK forecasts indicate that the UK fiscal deficit will fall below the 3% reference value in 2009/10, highlighting the exceptional temporary nature of the excess over the 3% reference value. The authorities also highlight: debt levels well below the reference level, which in their view allow flexibility for sustained investment in public services; commitments made to improve efficiency and value for money

in public spending; spending plans which allow for improvements in public services; significant commitments to implement the Lisbon Strategy for Jobs and Growth including on science spending, the Technology Programme and higher education teaching; and planned spending on Official Development Assistance (ODA).

The analysis presented above covers the items put forward by the authorities, except the observation by the authorities on the UK's international aid commitments. Under the latter item, the authorities record the UK's programme to increase its international development contributions, particularly in the context of the EU's collective commitment to provide an average of 0.56% of Gross National Income as Official Development Assistance by 2010. The UK plans to reach that level in 2010/11.

In 2005 and 2006, the ratio of the UK's net Official Development Assistance to Gross National Income (GNI) stood at 0.47% and 0.51% respectively<sup>12</sup>. The ODA figures for those two years included the debt relief given to Nigeria which was agreed by the Paris Club group of creditors. In 2007, ODA fell to 0.36%, of GNI reflecting the lower levels of debt relief.

#### **4.4. Other factors considered relevant by the Commission**

The Commission services' spring 2008 forecast assumes that the non-cyclical primary expenditure plans that were announced as part of the 2007 Comprehensive Spending Review will be adhered to. However, during the six years between 2002/03 and 2007/08, annual *total* expenditure outturns have exceeded the *original* total spending envelopes that had been established in previous Spending Reviews. Past trends show nevertheless that typically expenditure overruns are smaller in the first year of the spending review period, suggesting that the risks from higher than planned expenditure are relatively smaller for the deficit forecast for 2008/09 but will increase in 2009/10.

The nationalisation on the 22 February 2008 of Northern Rock bank, which had been facing severe liquidity problems since September 2007 as a result of the credit squeeze, did not have any direct effect on the general government accounts for the time being. However, it is not yet fully clear whether the Bank of England's loan to the bank, which stood at £24.1 billion or 1.7% of GDP at end-March 2008, should have already been reported as government debt, since it was granted on behalf of the State and with State guarantee. This is currently being discussed between the UK's Office for National Statistics (ONS) and Eurostat. Meanwhile, the Bank of England's liquidity support and the Treasury's guarantees to the bank's other creditors (about £30 billion or 2.0% of GDP) remain a contingent liability.

The accounting treatment of some Public-Private Partnership (PPP) contracts is subject to an ongoing discussion between Eurostat and the ONS<sup>13</sup>. The Commission is aware that the UK authorities aim to adopt International Financial Reporting Standards for the preparation of the annual financial statements of government departments and other public bodies from 2009/10. This move could see some of the current Private Finance Initiative (PFI) projects that are off-balance-sheet reclassified onto the public sector's books. Reclassifications would not necessarily adversely affect the general government accounts. Nevertheless, it remains possible that the changes in the accounting treatment, including any changes to comply with Eurostat's guidance on the accounting of PPPs in general government accounts, could lead to

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<sup>12</sup> Annex 1, 2008 Annual Report, Department for International Development. <http://www.dfid.gov.uk/pubs/files/departamental-report/2008/Annexes-bcov.pdf>

<sup>13</sup> See section 6.6 of the report on Eurostat's latest EDP visit to the UK: [http://epp.eurostat.ec.europa.eu/pls/portal/docs/PAGE/PGP\\_DS\\_GFS/PGE\\_DS\\_GFS\\_9/FINDINGS%20FROM%20THE%20MISSION%20TO%20THE%20UK%20ON%2025-26%20JANUARY%202007\\_WEBSITE.PDF](http://epp.eurostat.ec.europa.eu/pls/portal/docs/PAGE/PGP_DS_GFS/PGE_DS_GFS_9/FINDINGS%20FROM%20THE%20MISSION%20TO%20THE%20UK%20ON%2025-26%20JANUARY%202007_WEBSITE.PDF)

a small increase in the general government deficit estimate in 2009/10, depending *inter alia* on the share of off-balance sheet PPPs that would end up on the general government accounts.

In its opinion on the most recent update of the convergence programme<sup>14</sup>, the Council concluded that the programme confirmed a significant deterioration in the United Kingdom's budgetary position that, coupled with a probably weaker macroeconomic context than envisaged, carried a clear risk that general government deficit would breach the 3% of GDP deficit reference value in the near term. The Council therefore invited the United Kingdom to implement measures necessary for the deficit not to exceed the reference value of 3% of GDP.

## 5. CONCLUSIONS

The general government deficit in the United Kingdom planned for 2008/09 as notified in March 2008 is 3.2% of GDP, above but close to the 3% of GDP reference value. The fiscal relaxation announced by the government in May 2008 is expected to raise the deficit ratio by an additional 0.2 percentage points in 2008/09. The planned excess over the reference value cannot be qualified as exceptional within the meaning of the Treaty and the Stability and Growth Pact. Furthermore, it cannot be considered temporary. This suggests that the deficit criterion in the Treaty is not fulfilled.

General government gross debt remains below the 60% of GDP reference value. The debt criterion in the Treaty is fulfilled.

In line with the Treaty, this report has also examined "relevant factors". Given that the deficit does not satisfy the double condition of closeness and temporariness, these factors cannot according to the Stability and Growth Pact be taken into account in the steps leading to the decision on the existence of an excessive deficit.

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<sup>14</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2008:049:0025:0028:EN:PDF>