IFS analysis of today’s public finance figures

Today the Office for National Statistics and HM Treasury published *Public Sector Finances March 2005*. We now have details of central government receipts, central government spending, public sector net investment, borrowing and debt for the whole of financial year 2004–05.

**Headline Comparisons**

- **Public sector surplus on the current budget** in 2004–05 was minus £16.6bn (i.e. in deficit) compared to the March 2005 Budget projection of minus £16.1bn (and the March 2004 Budget projection of minus £10.5bn).

- **Public sector net borrowing** in 2004–05 was £34.5bn compared to the March 2005 Budget projection of £34.4bn (and the March 2004 Budget projection of minus £32.9bn).

- **Central government current receipts** in March were 4.6% higher than in the same month last year. Overall, current receipts in 2004–05 are thought to have been £419.2bn, compared to the March 2005 Budget projection of £419.5bn (and the March 2004 Budget projection of minus £422.4bn).

- **Central government current spending** in March was 1.6% lower than in the same month last year. Overall, current spending in 2004–05 is now thought to have been £434.2bn compared to the March 2005 Budget projection of £435.5bn (and the March 2004 Budget projection of minus £432.2bn).

- **Public sector net investment** in March was 23.0% higher than in the same month last year. Overall, net investment in 2004–05 is now thought to have been £17.8bn compared to the March 2005 Budget projection of £18.3bn (and the March 2004 Budget projection of £22.4bn).

The 2004–05 outturns and the golden rule

The Chancellor is committed to planning fiscal policy in line with his two fiscal rules. The first of these, the golden rule, requires that public sector current spending be met entirely out of public sector receipts over the course of an economic cycle – in other words, that the public sector current budget be at least in balance. The present economic cycle, which began in 1999–2000, is expected by the Treasury to end in 2005–06.

If, as Morgan Stanley argued in the January 2005 IFS Green Budget, the economic cycle came to a close in 2004–05, then the golden rule was met with £10bn to spare. However, this would mean that the economy would be broadly on trend during 2005–06 and yet the Treasury is expecting a deficit of £5.7bn on the current budget. This could pose
problems for the ability of the golden rule to be met over the new economic cycle without further tax raising measures.

If the Treasury is correct, and the economic cycle ran from 1999–2000 to 2005–06, then the golden rule will be met over the current economic cycle as long as the current budget is not in deficit by more than £9.6bn in 2005–06. The March 2005 Budget forecast is for a current budget deficit of £5.7bn, while the January 2005 IFS Green Budget forecast is for a £13.4bn deficit. The average absolute forecasting error made one year ahead by the Treasury in the past is equivalent to £15bn in today’s terms. On the basis of previous Treasury forecasting errors we estimate that if the March 2005 Budget forecast is the best available forecast then the probability that the golden rule will be met over the economic cycle ending in 2005–06 would be 59.9%, while if the January 2005 IFS Green Budget is the best available forecast then the corresponding figure would be 40.4%.

Christine Frayne, a senior research economist at the IFS said:

“Today’s public finance numbers largely confirmed the forecasts for 2004–05 contained in the March 2005 Budget. If the economic cycle ran from 1999–2000 to 2004–05 then the golden rule has been met over that period. If, as the Treasury expects, the cycle runs to 2005–06 then it could go either way, but the rule seems likely to be met or missed by a relatively small margin. Of greater economic importance is the strength of the public finances looking forwards. The Treasury forecasts imply that the Government’s spending plans can be financed, and the golden rule expected to be met with caution, without any further announcements of tax increases. In contrast the forecasts in the January 2005 IFS Green Budget imply that new tax increases of £11bn would be required. This is largely due to weaker expected growth in tax receipts, a concern that was echoed this week by the International Monetary Fund.”

**Further Analysis**

**Central government current receipts**

Overall, central government current receipts in 2004–05 came in £0.3bn lower than the projection in the March 2005 Budget (and £3.2bn lower than the forecast made in the March 2004 Budget).

Income tax receipts (net of income tax credits and including receipts of capital gains tax) are now thought to have been £125.1bn, compared to the March 2005 Budget forecast of £125.0bn (and the March 2004 Budget forecast of £125.6bn¹).

Corporation tax receipts (net of company tax credits) are now thought to have been £33.5bn, compared to the March 2005 Budget forecast of £33.6bn (and the March 2004 Budget forecast of £34.4bn¹).

Receipts of National Insurance Contributions are now thought to have been £78.1bn, compared to the March 2005 Budget forecast of £77.9bn (and the March 2004 Budget forecast of £77.7bn).

Value Added Tax receipts are now thought to have been £73.0bn, compared to the March 2005 Budget forecast of £72.3bn (and the March 2004 Budget forecast of £73.1bn).
Central government current spending

Overall, central government current spending (including depreciation) in 2004–05 came in £1.3bn lower than the projection in the March 2005 Budget (and £2.0bn higher than the forecast made in the March 2004 Budget).

Spending on net social benefits is now thought to have been £128.3bn, compared to the March 2005 Budget forecast of £128.1bn (and the March 2004 Budget forecast of £129.7bn).

Spending on debt interest payments is now thought to have been £23.9bn, compared to the March 2005 Budget forecast of £23.8bn (and the March 2004 Budget forecast of £23.9bn).

Other current spending by central government, including spending on the delivery of public services, is now thought to have been £282.0bn, compared to the March 2005 Budget forecast of £283.6bn (and the March 2004 Budget forecast of £278.6bn).

Relevant links:
This, and previous editions of this press release, can be downloaded from http://www.ifs.org.uk/press/pub_fin.shtml

Useful links and background information on the Budget can be found at http://www.ifs.org.uk/budgets/budget2005/index.php


HM Treasury, Budget 2005: http://www.hm-treasury.gov.uk/budget/budget_05/bud_bud05_index.cfm


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Notes to editors:
1. Adjusted for our estimate of the March 2004 Budget forecast for the relevant tax credits.
2. Central government current spending includes depreciation.
3. Where possible we compare figures on an accruals basis with the HM Treasury forecast.