IFS analysis of today’s public finance figures

Today the Office for National Statistics and HM Treasury published Public Sector Finances March 2007. We now have details of central government receipts, central government spending, public sector net investment, borrowing and debt for the whole of financial year 2006–07.

Gemma Tetlow, a research economist at the IFS, said:

“Today’s figures show that Gordon Brown’s golden rule has been met with almost £10 billion to spare over the 10-year economic cycle that the Treasury currently estimates to have run from 1997–98 to 2006–07. Subsequent revisions to estimates of spending and revenues may change the estimated size of the cumulative current budget surplus over this period, but are unlikely to eliminate it entirely. This suggests that we can be fairly confident that the rule will ‘stay met’ unless new national accounts data force the Treasury to re-date the economic cycle.

The rule has been met in part because of the Chancellor’s debateable decision in summer 2005 to move the start date of the economic cycle two years earlier. Had this not been done, the rule would have been broken by £3.5 billion over the eight-year cycle that would have begun in 1999–2000. Although such a breach would have had no direct economic significance in an economy now generating £1,300 billion a year in national income, it would clearly have been embarrassing for the Chancellor given his determination to meet the letter as well as the spirit of the rule. But, standing back from the precise definition of the rule, over the past decade the Government has by and large raised enough in tax revenue to cover its day-to-day spending and has only borrowed to finance investment.

Unfortunately, the re-dating of the cycle and the delay in announcing fresh tax increases and cuts in public spending as a share of national income until after the 2005 election may have undermined the credibility of the fiscal framework. The beginning of a new economic cycle, and the likely arrival of a new Chancellor at Number 11, would seem a sensible time to tweak the fiscal framework for the better and to try to help restore credibility. In particular, the golden rule should be made more forward-looking, less reliant on our ability to date the economic cycle, and should take explicit account of the significant uncertainty around any fiscal forecast. The Treasury should also consider what measures it can take to boost confidence that future forecasts of the public finances will not be made overoptimistic to delay painful tax and spending decisions.

In relation to the sustainable investment rule, the Treasury is yet to announce whether they will continue to aim to keep net debt below 40% of national income. In addition, the Treasury should assess whether a broader measure of the public sector’s indebtedness, for example to include more PFI or public sector pension liabilities, and a suitably higher debt ceiling would be more appropriate.”
Headline Comparisons

- **Public sector surplus on the current budget** in 2006–07 was minus £8.8bn (i.e. in deficit) compared to the March 2007 Budget projection of minus £9.5bn (and the March 2006 Budget projection of minus £7.0bn).

- **Public sector net borrowing** in 2006–07 was £33.6bn compared to the March 2007 Budget projection of £35.0bn (and the March 2006 Budget projection of £35.8bn).

- **Public sector net debt** at the end of 2006–07 was £501.0bn, or 37.4% of national income compared to the March 2007 Budget projection of 37.2% (and the March 2006 Budget projection of 37.5%).

- **Central government current receipts** in March were 4.3% higher than in the same month last year and over the whole of 2006–07 were 6.6% above the outturn for 2005–06. Overall, current receipts in 2006–07 are thought to have been £482.2bn, compared to the March 2007 Budget projection of £482.1bn (and the March 2006 Budget projection of £480.9bn).

- **Central government current spending** in March was 4.5% higher than in the same month last year and over the whole of 2006–07 was 5.3% above the outturn for 2005–06. Overall, current spending in 2006–07 is now thought to have been £491.0bn compared to the March 2007 Budget projection of £490.9bn (and the March 2006 Budget projection of £487.2bn).

- **Public sector net investment** in March was 11.4% higher than in the same month last year and over the whole of 2006–07 was 9.6% above the outturn for 2005–06. Overall, net investment in 2006–07 is now thought to have been £24.9bn compared to the March 2007 Budget projection of £25.5bn (and the March 2006 Budget projection of £28.8bn).

Assessing compliance with the fiscal rules

The Chancellor’s ‘golden rule’ requires public sector current spending to be met entirely out of public sector receipts over the course of an economic cycle – in other words, that the public sector current budget should be in balance or surplus on average over the cycle. The government should only borrow to finance capital spending.

The Treasury estimates that an economic cycle began in the first half of 1997 and the Budget states that “the economy is expected to have returned to trend early in 2007”. This and other figures contained in the Budget imply that the Treasury now expects this cycle to include the fiscal years 1997–98 to 2006–07. The cumulative surplus over the years 1997–98 to 2006–07 is estimated to be £9.6bn. These initial outturns suggest that the golden rule will have been met over a ten year economic cycle beginning in 1997–98. Prior to July 2005, the Treasury assessed that the economic cycle began two years later, in 1999–2000. Including the fiscal years 1997–98 and 1998–99 in this cycle made the golden rule easier to meet. However at the time Mr Brown told the Treasury Select Committee that “we would meet the Golden Rule irrespective”. Today’s figures suggest that this has turned out not to be the case: had the economic cycle run for the eight years from 1999–2000, the golden rule would have been missed by £3.5bn. However, there is no direct economic impact of the difference between meeting the golden rule by a margin of
£9.6bn or missing it by £3.5bn over a period spanning several years and annual GDP expected to be around £1,300bn.

The sustainable investment rule states that “net public debt as a proportion of GDP will be held over the economic cycle at a stable and prudent level”. The government has said that over this economic cycle public sector net debt should be kept below 40% of GDP in each and every year. Apart from in 1997–98, when debt was at 41.6% of GDP, public sector net debt has been below 40% of GDP.

Further Analysis

Information is now available for the whole of 2006–07. The figures for receipts and spending in March 2007 show:

Central government current receipts

Overall, central government current receipts in 2006–07 came in £0.1bn higher than the projection in the March 2007 Budget (and £1.3bn higher than the forecast made in the March 2006 Budget).

Receipts of Income Tax, Capital Gains Tax and National Insurance Contributions are now thought to have been £234.2bn, compared to the March 2007 Budget forecast of £234.1bn (and the March 2006 Budget forecast of £232.8bn).

Cash receipts of Value Added Tax are now thought to have been £77.4bn, compared to the March 2007 Budget forecast of £77.3bn (and the March 2006 Budget forecast of £76.5bn).

Corporation tax receipts (net of company tax credits) are now thought to have been £44.3bn, compared to the March 2007 Budget forecast of £44.4bn (and the March 2006 Budget forecast of £48.4bn).

Central government current spending

Overall, central government current spending (including depreciation) in 2006–07 came in £0.1bn higher than the projection in the March 2007 Budget (but £3.8bn higher than the forecast made in the March 2006 Budget).

Spending on net social benefits is now thought to have been £132.3bn, compared to the March 2007 Budget forecast of £132.8bn (and the March 2006 Budget forecast of £131.5bn).

Spending on debt interest payments is now thought to have been £27.5bn, compared to the March 2007 Budget forecast of £27.4bn (and the March 2006 Budget forecast of £26.3bn).

Other current spending by central government, including spending on the delivery of public services, is now thought to have been £331.2bn, compared to the March 2007 Budget forecast of £330.7bn (and the March 2006 Budget forecast of £329.4bn).

Further information and contacts

For further information on today’s public finance release please contact: Carl Emmerson or Gemma Tetlow on 020 7291 4800, or email cemmerson@ifs.org.uk or gtetlow@ifs.org.uk.
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/budget2007/index.php

Office for National Statistics & HM Treasury, Public Sector Finances, March 2007:

The HM Treasury Budget 2007 is available at:
http://www.hm-treasury.gov.uk/budget/budget_07/bud_bud07_index.cfm

HM Treasury, Public Finance and Spending Statistics Index:
http://www.hm-treasury.gov.uk/economic_data_and_tools/finance_spending_statistics/finexp_index.cfm

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Notes to editors:

1. Central government current spending includes depreciation.
2. Where possible we compare figures on an accruals basis with the HM Treasury forecast.