IFS analysis of today’s public finance figures

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

Headline Comparisons

- **Central government current receipts** in November were 5.1% higher than in the same month last year. This month’s Pre-Budget Report forecast for 2006–07 implies an increase over last year’s levels of 6.9% for the year as a whole and of 7.3% for the period from November 2006 to March 2007. The latest figures show an increase over last year’s levels of 6.4% for the year to date.

- **Central government current spending** in November was 1.0% higher than in the same month last year. This month’s Pre-Budget Report forecast for 2006–07 implies an increase over last year’s levels of 5.0% for the year as a whole and of 2.6% for the period from November 2006 to March 2007. The latest figures show an increase over last year’s levels of 6.1% for the year to date.

- **Public sector net investment** in November was £2.2bn (8.9%) higher than in the same month last year. This month’s Pre-Budget Report forecast for 2006–07 implies an increase of 30.2% for the year as a whole and an increase of 16.1% for the period from November 2006 to March 2007. The latest figures show an increase over last year’s levels of 43.0% for the year to date.

Gemma Tetlow, a research economist at the IFS said:

“The Pre-Budget Report forecast that growth in central government spending would slow over the remainder of this financial year. Today’s figures show that this was the case in November, with a cash fall in spending on social security benefits and tax credits and much slower growth in other spending by central government, including that on public services. The Treasury now estimates that the current economic cycle began in 1997–98 and will end this financial year. Over this period it looks like the Government will receive sufficient revenue to cover its current expenditure and therefore Gordon Brown’s golden rule should be met over the economic cycle that the Treasury estimates is about to end.

Looking forwards the Chancellor expects the current budget to return to surplus from 2008–09 onwards and net debt to remain below 40% of national income throughout the forecast period. If his forecast for the current budget proves to be correct, the golden rule would also be met over the economic cycle beginning in 2006–07, provided the cycle runs for at least four years. Gordon Brown is yet to announce how the sustainable investment rule will be judged over the new economic cycle. If he defines compliance as ensuring that ‘net debt will be maintained below 40% of GDP in each and every year’, as it has been over the current economic cycle, then the sustainable investment rule would also be expected to be met, albeit with relatively little, and declining, room to manoeuvre.”
Assessing compliance with the golden rule

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 Pre-Budget Report states that “the Government’s judgement is that the current cycle started in 1997–98. Based on assumptions used in these projections the economy will return to its trend level, ending the current cycle in early 2007”. This and other figures contained in the Pre-Budget Report imply that Treasury now expects the cycle to run from 1997–98 to 2006–07. The cumulative surplus over the years from 1997–98 to 2005–06 is estimated to be £16.3bn, so the golden rule would be met if the deficit on the current budget is no more than £16.3bn in this financial year. This month’s Pre-Budget Report projected that the current budget would be in deficit by £7.9bn this year, which would mean that the golden rule would be met, albeit with just £8bn to spare over a 10 year cycle. So far this financial year the cumulative current budget deficit is running at 80% of the level that it was at this point last year. Should this trend continue over the remaining 4 months of the financial year, and there are reasons to think that there may be some improvement over the rest of the financial year, the current budget deficit for the whole of 2006–07 would be £11.8bn. This would mean the Chancellor would meet the golden rule over the current cycle with a margin of just £4.5bn.

Further Analysis

We should be cautious in inferring or extrapolating likely outcomes over the financial year as a whole from information on only the first eight months. Bearing this in mind, the figures for receipts and spending in November 2006 show:

Central government current receipts

Receipts of Income Tax, Capital Gains Tax and (net cash) National Insurance Contributions for November were 8.3% higher than in the same month last year. This month’s Pre-Budget Report forecast implies that the receipts from these taxes will be 6.8% up on last year’s levels over the whole year, and 8.2% up over the period from November 2006 to March 2007. The receipts for these taxes during the first eight months of 2006–07 were 5.9% higher than those for the same months in 2005–06.

Cash receipts of VAT in November were 7.9% higher than in the same month last year. This month’s Pre-Budget Report forecast implies that these receipts will be 4.6% up on last year’s levels over the whole year, and 4.4% up over the period from November 2006 to March 2007. During the first eight months of 2006–07 these receipts were 5.1% higher than those for the same months in 2005–06.

Corporation tax receipts for November 2006 were 31.0% higher than in the same month last year, although due the pattern of these receipts over the year, November is not usually a significant month. This month’s Pre-Budget Report forecast implies that these receipts will be 13.2% up on last year’s levels over the whole year, and 5.8% up over the period from November 2006 to March 2007. During the first eight months of 2006–07 these receipts were 18.2% higher than those for the same months in 2005–06.

Central government current spending

Expenditure on net social benefits was 4.7% lower in November 2006 than in November 2005. This month’s Pre-Budget Report forecast implies that this spending will be 4.0% up on last year’s levels over the whole year, and 3.5%
up over the period from November 2006 to March 2007. During the first eight months of 2006–07 this spending was 3.0% higher than in the same months in 2005–06.

Spending on debt interest (which is relatively small as a share of spending overall) was £2.2bn in November 2006 compared to £2.0bn in November 2005.

Other current spending by central government, including spending on the delivery of public services, was 3.2% higher in November 2006 than in November 2005. This month’s Pre-Budget Report forecast implies that this spending will be 5.4% up on last year’s levels over the whole year, and 1.6% up over the period from November 2006 to March 2007. During the first eight months of 2006–07 this spending was 7.6% higher than in the same months in 2005–06.

In November 2006, public sector net investment was £2.2bn compared to £2.0bn in the same month in 2005. So far in 2006–07, a total amount of £15.9bn has been spent on public sector net investment, compared to the £11.1bn that had been spent by the same point in 2005–06. This month’s Pre-Budget Report predicted that net investment in 2006–07 as a whole would be £28.9bn, which is 30.2% above last year’s level.

Further information and contacts
For further information on today’s public finance release please contact: Carl Emmerson, Christine Frayne or Gemma Tetlow on 020 7291 4800, or email cemmerson@ifs.org.uk or cfrayne@ifs.org.uk or gtetlow@ifs.org.uk.

The IFS Green Budget, which will again be in collaboration with Morgan Stanley, will be on Wednesday 31st January 2007. For more details please email bbrimstone@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 Pre-Budget Report can be found at http://www.ifs.org.uk/budgets/pbr2006/index.php
Office for National Statistics & HM Treasury, Public Sector Finances, November 2006:
HM Treasury, Pre-Budget Report 2006:
http://www.hm-treasury.gov.uk/pre_budget_report/prebud_pbr06/prebud_pbr06_index.cfm
HM Treasury, Public Finance Statistics Index:
http://www.hm-treasury.gov.uk/economic_data_and_tools/pubfinance/data_pubfinance_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.