IFS analysis of today’s public finance figures

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

Headline Comparisons

- **Central government current receipts** in December were 9.1% higher than in the same month last year. Last 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 7.1% for the period from November 2006 to March 2007. The latest figures show an increase over last year’s levels of 6.7% for the year to date and a 6.6% increase in November and December 2006 over the same two months last year.

- **Central government current spending** in December was 4.8% higher than in the same month last year. Last 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 2.7% 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 and a 4.0% increase in November and December 2006 over the same two months last year. The ONS/HMT press release notes that the allocation of central government spending over the nine months of the current financial year which have already elapsed will be revised next month, however, the fact that growth in spending since the Pre-Budget Report is running above that required to meet the Chancellor’s forecast is likely to remain.

- **Public sector net investment** in December was £0.9bn higher (56.1%) than in the same month last year. Last 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 17.4% for the period from November 2006 to March 2007. The latest figures show an increase over last year’s levels of 44.4% for the year to date and a 33.7% increase in November and December 2006 over the same two months last year.

Gemma Tetlow, a research economist at the IFS said:

“Today’s figures reveal that growth in central government spending in December, whilst slower than earlier in the financial year, is still ahead of that required for last month’s Pre-Budget Report projection to be met. In terms of the golden rule, this higher growth in spending was offset by similarly high growth in receipts in December, in particular VAT. The Treasury currently believes that an economic cycle ran from the first half of 1997 and will finish early this year. Based on receipts and spending from the financial year to date, the current budget is likely to be in deficit by
more than the £7.9 billion that the Pre-Budget Report forecast. However, the current budget deficit is extremely unlikely to exceed the Chancellor’s projection by more than £8.4 billion, which means that the golden rule should be met over the current economic cycle.”

IFS economists will be presenting their forecasts for the public finances for this year and the medium term on Wednesday 31st January in the Green Budget. This will enable us to predict whether the Chancellor is on course to meet the Golden Rule and the Sustainable Investment Rule over the next economic cycle. Please contact Bonnie Brimstone on bbrimstone@ifs.org.uk for more details.

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 the 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 £8.4bn to spare over a ten year cycle. So far this financial year the cumulative current budget deficit is running at 82% of the level that it was at this point last year. Should this trend continue over the remaining 3 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 £12.0bn. This would mean the Chancellor would meet the golden rule over the current cycle with a margin of just £4.3bn.

Further Analysis

Even with information available for three quarters of the current financial year, it is still important to be cautious in extrapolating over the whole year. Bearing this in mind the figures for December 2006 show:

Central government current receipts

Receipts of Income Tax, Capital Gains Tax and (cash) National Insurance Contributions for December were 4.9% higher than in the same month last year. Last 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 nine months of 2006–07 were 5.8% higher than those for the same months in 2005–06, while receipts for November and December 2006 were 6.4% higher than the same two months last year.
Cash receipts of VAT in December were 13.5% higher than in the same month last year. Last 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 nine months of 2006–07 these receipts were 5.9% higher than those for the same months in 2005–06, while receipts for November and December 2006 were 10.4% higher than the same two months last year.

Corporation tax receipts for December 2006 were 23.6% higher than in the same month last year, although due the pattern of these receipts over the year, December is not usually a significant month. Last 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 nine months of 2006–07 these receipts were 18.6% higher than those for the same months in 2005–06, while receipts for November and December 2006 were 26.0% higher than the same two months last year.

**Central government current spending**

The ONS/HMT press release notes that the allocation of central government spending over the nine months of the current financial year which have already elapsed will be revised next month, however, the fact that growth overall central government spending since the Pre-Budget Report is running above that required to meet the Chancellor’s forecast is likely to remain.

Expenditure on net social benefits was 4.2% higher in December 2006 than in December 2005. Last 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 3.0% up over the period from November 2006 to March 2007. During the first nine months of 2006–07 this spending was 3.7% higher than in the same months in 2005–06, while spending November and December 2006 were 0.2% higher than the same two months last year.

Spending on debt interest (which is relatively small as a share of spending overall) was £2.2bn in December 2006 compared to £2.1bn in December 2005.

Other current spending by central government, including spending on the delivery of public services, was 4.9% higher in December 2006 than in December 2005. Last 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 1.9% up over the period from November 2006 to March 2007. During the first nine months of 2006–07 this spending was 7.4% higher than in the same months in 2005–06, while spending for November and December 2006 were 5.3% higher than the same two months last year.

In December 2006, **public sector net investment** was £2.5 bn compared to £1.6 bn in the same month in 2005. So far in 2006–07, a total amount of £18.4 bn has been spent on public sector net investment, compared to the £12.7 bn that had been spent by the same point in 2005–06. Last month’s Pre-Budget Report predicted that net investment in 2006–07 would be £28.9 bn, 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


HM Treasury, Pre-Budget Report 2006: http://www.hm-treasury.gov.uk/pre_budget_report/prebud_pbr06/prebud_pbr06_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.