IFS analysis of today’s public finance figures

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

Headline Comparisons

- **Central government current receipts** in May were 5.5% higher than in the same month last year. Receipts in April and May 2004 were 3.7% higher than in the same months of 2003. The 2004 Budget implied that central government current receipts for the whole of 2004–05 would be 7.4% above 2003–04 levels.

- **Central government current spending** in May was 3.1% higher than in the same month last year. Spending in April and May 2004 was 5.6% higher than in the same months of 2003. The 2004 Budget implied that central government current spending for the whole of 2004–05 would be 5.3% above 2003–04 levels.

- **Public sector net investment** in May was £0.4bn, or 69.7% higher than in the same month last year. Together, public sector net investment during April and May 2004 has been £0.7bn, which is 62.8% lower than in the same two months of 2003. The Budget predicted that net investment in 2004–05 would be £22.4bn, which is 56.6% above last year’s level.

Further Analysis

Little can be inferred or extrapolated about the public finances in 2004–05 from information about only the first two months of the financial year. Bearing this in mind, the figures for receipts and spending in May 2004 show:

**Central government current receipts**

Income tax and Capital Gains Tax receipts for May 2004 were 2.3% higher than in the same month last year. Together, the receipts for these taxes during the first two months of 2004–05 were 1.4% lower than those for the first two months of 2003–04. The Budget forecasts imply that these taxes’ receipts will grow by 7.2% over the whole of 2004–05.

Corporation tax receipts for May 2004 were 5.4% higher than in the same month last year. Corporation tax receipts for April and May 2004 were 13.3% higher than those for the same two months last year. The Budget forecast implies that Corporation tax receipts will grow by 21.4% over the whole of 2004–05.
VAT receipts in May 2004 were 4.2% higher than the same month last year. VAT receipts for April and May 2004 were 12.1% higher than those for the same two months in 2003. The Budget forecast implies that VAT receipts will grow by 5.8% over the whole of 2004–05.

In May 2004, cash receipts of social security contributions grew by 11.4% over last May’s level, while accrued social security contributions grew by 1.1%. Comparing the first two months of this financial year to the same months of 2003, the figures are 13.0% and 0.5% respectively. The Budget forecast implies that social security contributions will grow by 7.6% over the whole of 2004–05.

**Central government current spending**

Expenditure on net social benefits was 3.5% higher in May 2004 than in May 2003. Expenditure during April and May 2004 was 5.4% higher than in the same months of 2003. The Budget forecast implies that central government net social benefit expenditure will grow by 6.8% over 2004–05.

Spending on debt interest (which is relatively small as a share of spending overall) was 4.2% lower in May 2004 than in May 2003.

Other current spending by central government, including spending on the delivery of public services, was 3.6% higher in May 2004 than in May 2003. Comparing the first two months of 2004–05 with the first two months of 2003–04, the figure is 6.3%. The Budget forecast implies that this component of spending will grow by 4.5% over the year as a whole.

In May 2004, public sector net investment was £0.4bn compared to £0.3bn in the same month in 2003. So far in 2004–05, a total amount of £0.7bn has been spent on public sector net investment, compared to the £1.8bn that had been spent by the same point in 2003–04. The total value of public sector net investment expected in 2004–05 according to Budget 2004 forecasts is £22.4bn, which is 56.6% higher than the total for 2003–04.

**The effects of raised oil prices on the public finances**

Higher oil prices affect tax revenues by raising the tax receipts from North Sea Oil taxes; they also have an indirect effect if they depress economic activity and reduce revenues from other taxes. The assumption made about oil prices in Budgets and Pre-Budget Reports depends on how the price at the time of the forecast compares to the average of the latest independent forecasts. If the former exceeds the latter, the independent forecast is used and projected to remain constant in real terms. If the actual price is below the forecast, the actual price is used instead. In March 2004, at the time of the Budget, the average of the independent forecasts was an oil price of $27.4/barrel in 2004 and $26.6/barrel in 2005. The assumption used by the Treasury was that oil prices would be $27.4/barrel this year and would remain the same in real terms thereafter. In June 2004, the most recent independent forecasts have an average of $32.3/barrel in 2004 and $29.1/barrel in 2005. According to the most recent NAO audit of the oil price assumption, the Treasury estimates that a 5% increase in the oil price would, other things being equal, increase revenues by about £220m in the first year and £270m in the next. The latest 2004 forecast is about 17.9% higher than the Budget one but the majority of the oil price increase is expected to be temporary. This suggests that, given the Treasury’s estimates of the revenue effects of oil prices, there may be about £800m of extra revenue this year, £200m
next year and smaller gains thereafter. The gains are of short duration because prices are expected to fall by 2005 most of the way back to previously expected levels.

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

“It is very early days, but so far this financial year central government tax receipts are only rising half as quickly as the Chancellor forecast in March's Budget. As Mervyn King emphasised earlier this week, the Treasury is relying on this expected increase in revenues to swing us back to a sustainable fiscal position. If revenues do not recover as strongly as the Treasury expects, fresh tax increases will need to be announced to finance the government's spending plans and ensure that the Chancellor's fiscal rules continue to be met.”

Further information and contacts
For further information on today’s public finance release please contact: Robert Chote or Christine Frayne on 020 7291 4800, or email rchote@ifs.org.uk or cfrayne@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/budgetindex.shtml
Office for National Statistics & HM Treasury, Public Sector Finances, May 2004:
The IFS Green Budget, January 2004:
HM Treasury, Budget 2004:
http://www.hm-treasury.gov.uk/budget/bud_bud04/bud_bud04_index.cfm
HM Treasury, Pre-Budget Report 2003 is available at:
http://www.hm-treasury.gov.uk/pre_budget_report/prebud_pbr03/prebud_pbr03_index.cfm
HM Treasury, Public Finance Statistics Index:
http://www.hm-treasury.gov.uk/economic_data_and_tools/pubfinance/data_pubfinance_index.cfm

ENDS

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.