IFS analysis of today’s public finance figures

Today the Office for National Statistics and HM Treasury published *Public Sector Finances April 2004*. We now have details of central government receipts, central government spending, public sector net investment, borrowing and debt for the first month of financial year 2004–05 and revised details for the whole of financial year 2003–04.

**Headline Comparisons**

- **Public sector surplus on current budget** in 2003–04 is now estimated to be minus £17.2bn (i.e. in deficit), compared to the March 2004 Budget estimate of minus £21.3bn.

- **Public sector net borrowing** in 2003–04 is now estimated to be £33.1bn, compared to the £37.5bn estimate in the Budget.

- **Central government current receipts** in April were 4.0% higher than in the same month last year. The 2004 Budget implied that central government current receipts for the whole of 2004–05 would be 7.3% above 2003–04 levels.

- **Central government current spending** in April was 8.6% higher than in the same month last year. The 2004 Budget implied that central government current spending for the whole of 2004–05 would be 5.4% above 2003–04 levels.

- **Public sector net investment** in April was £0.5bn, or 65.9% lower than in the same month last year. The Budget predicted that net investment in 2004–05 would be £22.4bn, which is 41.3% 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 month of the financial year. Bearing this in mind, the figures for receipts and spending in April 2004 show:

**Central government current receipts**

Income tax and Capital Gains Tax receipts for April 2004 were 3.8% lower than in the same month last year. The Budget forecasts imply that these taxes’ receipts will grow by 8.0% over the whole of 2004–05.

Corporation tax receipts for April 2004 were 14.2% higher than in the same month last year. The Budget forecast implies that Corporation tax receipts will grow by 21.4% over the whole of 2004–05.

VAT receipts in April 2004 were 18.2% higher than the same month last year. The Budget forecast implies that VAT receipts will grow by 5.8% over the whole of 2004–05.
In April 2004, cash receipts of social security contributions grew by 14.6% over last April’s level, while accrued social security contributions grew by 5.1%. The Budget forecast implies that social security contributions will grow by 7.8% over the whole of 2004–05.

Central government current spending

Expenditure on net social benefits was 8.5% higher in April 2004 than in April 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 1.5% higher in April 2004 than in April 2003.

Other current spending by central government, including spending on the delivery of public services, was 9.3% higher in April 2004 than in April 2003. The Budget forecast implies that this component of spending will grow by 4.6% over the year as a whole.

In April 2004, public sector net investment was £0.5bn compared to £1.5bn in the same month in 2003. The total value of public sector net investment expected in 2004–05 by the Budget is £22.4bn, which is 41.3% higher than the total for 2003–04.

The 2003–04 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. The average surplus over the seven years of the cycle was expected in Budget 2004 to be 0.1% of national income, while the current budget in 2003–04 was expected to be in deficit by £21.3bn, or 1.9% of national income. Today’s revisions show that the actual current budget deficit in 2003–04 was £17.2bn, or 1.5% of national income. If the Budget predictions for the 2004–05 and 2005–06 current budget outturns prove accurate, the average current budget surplus over this economic cycle will be about 0.2% of national income. This corresponds to a total margin for error of £13.1bn in 2005–06 pounds, which is approximately a £5bn increase on the margin that was expected in the Budget and a £2bn increase on the margin implied by last month’s Public Sector Finances figures.

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. 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 May 2004, the most recent independent forecasts have an average of $31.1/barrel in 2004 and $28.4/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 13.5% 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 £600m of extra revenue this year, £200m the next and negligible gains thereafter. The gains are of short duration because prices are expected to fall by 2005 almost the whole way back to previously expected levels.

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

“Revisions to last year’s figures have, for the second month running, increased the government’s margin of error on meeting the golden rule over the current economic cycle. This will be welcome by the Treasury as the room for manoeuvre was, and remains, tight given that there are still two years of the cycle to go. Concerns about the ability of the public finances to comply with the golden rule over the next economic cycle without further tax increases or further reductions in the planned growth in public spending remain. While the recent increases in the oil prices will boost revenues, this is expected to be a largely temporary rather than a permanent increase.”

Further information and contacts
For further information on today’s public finance release please contact: Carl Emmerson or Christine Frayne on 020 7291 4800, or email cemmerson@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, April 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
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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.