IFS analysis of today’s public finance figures

Today the Office for National Statistics and HM Treasury published Public Sector Finances April 2007. 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 2007–08 and revised details for the whole of financial year 2006–07.

Carl Emmerson, a deputy director at the IFS, said:

“Today’s figures show that the public sector current budget in April 2006 was £0.2bn in surplus, compared to a £0.9bn deficit in April 2006. However as we are only one month into financial year 2007–08 very little can be it inferred about the trajectory of the public finances over the whole year. Revisions to previous estimates suggest that Gordon Brown’s golden rule has been met with around £10 billion to spare over the 10-year economic cycle that the Treasury currently estimates to have run from 1997–98 to 2006–07. While further revisions to estimates of spending and revenues may change the estimated size of the cumulative current budget surplus over this period, but they 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 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 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 is now estimated to have been minus £7.6bn (i.e. in deficit) compared to last month’s estimates which suggested a deficit of £8.8bn, 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 is now estimated to have been £33.8bn compared to last month’s estimates which suggested borrowing of £33.6bn, 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 is now estimated to have been £501.4bn, or 37.4% of national income, unchanged from last month’s estimates and compared to the March 2007 Budget projection of 37.2% (and the March 2006 Budget projection of 37.5%).

- **Central government current receipts** in April were 4.1% higher than in the same month last year. The 2007 Budget implied that central government current receipts for the whole of 2007–08 would be 6.9% above 2006–07 levels.

- **Central government current spending** in April was 4.8% higher than in the same month last year. The 2007 Budget implied that central government current spending for the whole of 2007–08 would be 5.7% above 2006–07 levels.

- **Public sector net investment** in April was £1.3bn compared to £2.0bn in the same month last year. The Budget predicted that net investment in 2007–08 would be £29.4bn, which is 12.3% above last year’s level.

**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 £10.0bn in 2006–07 terms (or £10.6bn in 2007–08 terms). This is higher than the £9.6bn implied by last month’s data, which is due to revisions to receipts from business rates and to estimates of Local Authorities income and expenditure from housing services. These 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”. These 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 £2.7bn in 2006–07 terms (or £2.9bn in 2007–08 terms). However, there is no direct economic impact of the difference between meeting the golden rule by a margin of £10bn or missing it by £3bn over a period spanning several years and annual GDP (in 2006–07) 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

Little can be inferred or extrapolated about the public finances in 2007–08 from information about only the first month of the financial year. Bearing this in mind, the figures for receipts and spending in April 2006 show:

**Central government current receipts**

Receipts from Income tax, Capital Gains Tax and National Insurance Contributions for April 2007 were 4.4% higher than in the same month last year. The Budget forecasts imply that these taxes’ receipts will grow by 7.7% over the whole of 2007–08.

VAT receipts in April 2007 were 10.6% higher than the same month last year. The Budget forecast implies that VAT receipts will grow by 3.4% over the whole of 2007–08.

Corporation tax receipts for April 2007 were 3.1% higher than the same month last year. The Budget forecast implies that Corporation tax receipts will grow by 11.7% over the whole of 2007–08.

**Central government current spending**

Expenditure on net social benefits was 7.3% higher in April 2007 than in April 2006. The Budget forecast implies that central government net social benefit expenditure will grow by 5.7% over 2007–08.

Spending on debt interest (which is relatively small as a share of spending overall) was £2.6bn in April 2007 compared to £2.2bn in April 2006.

Other current spending by central government, including spending on the delivery of public services, was 3.1% higher in April 2007 than in April 2006. The Budget forecast implies that this component of spending will grow by 5.6% over the year as a whole.

Further information and contacts

For further information on today’s public finance release please contact: Robert Chote or Carl Emmerson on 020 7291 4800, or email rchote@ifs.org.uk or cemmerson@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


The HM Treasury Budget 2007 is available at: http://www.hm-treasury.gov.uk/budget/budget_07/bud_bud07_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.