IFS analysis of today’s public finance figures

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

**Headline Comparisons**

- **Central government current receipts** in October were 5.9% higher than in the same month last year. Receipts in the first seven months of this financial year were 6.3% higher than in the same period of 2003–04. The 2004 Budget implied that central government current receipts for the whole of 2004–05 would be 7.8% above 2003–04 levels.

- **Central government current spending** in October was 8.2% higher than in the same month last year. Spending in the first seven months of this financial year was 6.6% higher than in the period of 2003–04. The 2004 Budget implied that central government current spending for the whole of 2004–05 would be 5.2% above 2003–04 levels.

- **Public sector net investment** in October was £1.1bn, or 20.9% higher than in the same month last year. Together, public sector net investment during the first seven months of this financial year has been £6.9bn, which is 13.1% higher than in the same period of 2003–04. The Budget predicted that net investment in 2004–05 would be £22.4bn, which is 63.3% above last year’s level.

Commenting on today’s numbers Christine Frayne, a Senior Research Economist at the IFS, said:

“Gordon Brown will have to deliver the Pre-Budget Report in a fortnight’s time with the current budget deficit up on last year rather than halving as he had hoped at the time of the Budget in March. Today’s figures show the deficit moving further away from the Budget forecast for the third month in a row. If the trends seen so far this year continue, and it is still early days, the current budget deficit for 2004–05 would overshoot the Treasury forecast by more than £12bn. This would not be a particularly big error by historic standards, but it would be the fourth year running that the Treasury had erred in the same unfavourable direction.

On current trends, the Chancellor is on course to break his golden rule over the present economic cycle. (The golden rule states that the current budget – tax revenues minus non-investment spending – should be in balance or surplus over the ups and downs of the economic cycle, which the Treasury regards as running from 1999–2000 to 2005–06). The Bank of England and other independent commentators have suggested that spare capacity in the economy may have been used up more quickly than the Budget projected, so we may already be in the last year of the cycle. But although this would make it easier to hit the golden rule over this cycle on current trends, there would still only be a
50-50 chance of success. It would also make the rule harder to meet in the next cycle without fresh tax rises or spending cuts.

Today’s revenue figures will have been especially disappointing for the Treasury, as they show particularly weak Corporation Tax receipts in the most important month of the year for that tax. If the Treasury’s Budget forecast for Corporation Tax is to be fulfilled, revenues in the last five months of the year will have to be 41.9% up on the same period last year compared to the increase of just 12.5% we have seen over the year to date. A significant shortfall would cast further doubt on the Treasury’s relatively optimistic projections for Corporation Tax revenues over the next few years. On a more positive note, income tax receipts have picked up since the Summer with the most important months for this tax still to come in January and February.”

Further Analysis

With information available for only the first seven months of the current financial year, it is important to be cautious in extrapolating over the year. Bearing this in mind the figures for receipts and spending in October 2004 show:

Central government current receipts

Income tax and Capital Gains Tax receipts for October 2004 were 11.6% higher than in the same month last year. Together, the receipts for these taxes during the first seven months of 2004–05 were 5.7% higher than those for the first seven months of 2003–04. The Budget forecasts imply that these taxes’ receipts will grow by 7.4% over the whole of 2004–05.

Corporation tax receipts for October 2004 were 7.6% higher than in the same month last year. Corporation tax receipts for the first seven months of this financial year were 12.5% higher than those for the same seven months last year. The Budget forecast implies that corporation tax receipts will grow by 21.6% over the whole of 2004–05.

VAT receipts in October 2004 were 4.2% higher than the same month last year. VAT receipts for the first seven months of this financial year were 6.2% higher than those for the same period in 2003–04. The Budget forecast implies that VAT receipts will grow by 5.9% over the whole of 2004–05.

In October 2004, accrued receipts of social security contributions grew by 2.6% over last October’s level; for the first seven months of this financial year they were 2.4% higher than in the same period in 2003. The Budget forecast implies that social security contributions will grow by 3.5% over the whole of 2004–05.

Central government current spending

Expenditure on net social benefits was 6.3% higher in October 2004 than in October 2003. Expenditure during the first seven months of this financial year was 7.0% higher than in the same period of 2003–04. The Budget forecast implies that central government net social benefit expenditure will grow by 6.5% over 2004–05.

Spending on debt interest (which is relatively small as a share of spending overall) was 4.6% higher in October 2004 than in October 2003. In the year to date it has grown by 2.8% over the first seven months of last year, whereas the Budget forecast implies a 7.6% increase for the year as a whole.
Other current spending by central government, including spending on the delivery of public services, was 9.5% higher in October 2004 than in October 2003. Comparing the first seven months of 2004–05 with the first seven months of 2003–04, the figure is 6.7%. The Budget forecast implies that this component of spending will grow by 4.4% over the year as a whole.

**What would happen if these trends continued?**

Under the assumption that borrowing in the first seven months of 2004–05 as a proportion of the year’s total is the same as it was in 2003–04 then:

- **Public Sector Net Borrowing** would be around £39bn. This is compared to the Budget 2004 forecast of £32.9bn.

- **Current Budget** would be in deficit by around £23bn. This is compared to the Budget 2003 forecast of a deficit of £10.5bn.

It should be remembered that the average absolute error in forecasting one year ahead has been £12.1bn. So an error of the magnitude implied by extrapolating from these trends would not be particularly large by historical standards.

The Pre-Budget Report will be on Thursday the 2nd of December. An IFS briefing will be held at on Friday 3rd December. The briefing is free of charge and will take place at 1pm at our offices in Ridgmount Street. If you wish to attend please contact our conference organiser Bonnie Brimstone (bbrimstone@ifs.org.uk).

**Further information and contacts**

For further information on today’s public finance release please contact: Robert Chote, Carl Emmerson or Christine Frayne on 020 7291 4800, or email rchote@ifs.org.uk, 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](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](http://www.ifs.org.uk/budgetindex.shtml)

Office for National Statistics & HM Treasury, Public Sector Finances, October 2004:


HM Treasury, Public Finance Statistics Index:

[http://www.hm-treasury.gov.uk/economic_data_and_tools/pubfinance/data_pubfinance_index.cfm](http://www.hm-treasury.gov.uk/economic_data_and_tools/pubfinance/data_pubfinance_index.cfm)

HM Treasury, Pre-Budget Report 2004 will be available at:

[http://www.hm-treasury.gov.uk/pre_budget_report/prebud_pbr04/prebud_pbr04_index.cfm](http://www.hm-treasury.gov.uk/pre_budget_report/prebud_pbr04/prebud_pbr04_index.cfm)

HM Treasury, Budget 2004:

[http://www.hm-treasury.gov.uk/budget/bud_bud04/bud_bud04_index.cfm](http://www.hm-treasury.gov.uk/budget/bud_bud04/bud_bud04_index.cfm)

The IFS Green Budget, January 2004:

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.