IFS Green Budget 2016

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To make good decisions, understand your finances

Five years of Whole of Government Accounts (WGA)
- Provides insights not available from the National Accounts
- But – takes too long to produce
  - lack of comprehensive monthly financial reports

Infrastructure funding
- The Chancellor’s dilemma – how to improve the public finances and increase investment at the same time
- How hard is it to encourage private sector investment?
- Is it time to bring PFI on balance sheet?
- And instead prioritise investments that pay for themselves?
Five years of integrated financial accounts

Revenue & Expenditure

Comprehensive Income

Movements In Financial Position

Cash Flow Statement

Balance Sheet
Five years of Whole of Government Accounts

Revenue & Expenditure for 2013–14

- Revenue: £648bn
- Expenditure:
  - Operating expenditure: £718bn
  - Net finance costs: £79bn
- Accounting deficit: £149bn

Balance Sheet at 31 March 2014

- Assets:
  - Property, plant & equipment: £763bn
- Liabilities:
  - Debt: £1,451bn
  - Pensions: £1,302bn
  - Other liabilities: £436bn
- Net liabilities: £1,852bn

Net revenue: £648bn
Net expenditure: £718bn
Net accounting deficit: £149bn
Net finance costs: £79bn
Net liabilities: £1,852bn
Net assets: £574bn

Five years of accounting deficits

* Accounting deficits in 2009-10 and 2010-11 exclude one-off items.
Five years of balance sheets

<table>
<thead>
<tr>
<th>Year</th>
<th>Liabilities</th>
<th>Assets</th>
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<tbody>
<tr>
<td>2009-10</td>
<td>£1.2 trillion</td>
<td>£2.5 trillion</td>
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<tr>
<td>2010-11</td>
<td>£1.2 trillion</td>
<td>£2.4 trillion</td>
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<tr>
<td>2011-12</td>
<td>£1.3 trillion</td>
<td>£2.6 trillion</td>
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<td>2012-13</td>
<td>£1.3 trillion</td>
<td>£2.9 trillion</td>
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<tr>
<td>2013-14</td>
<td>£1.3 trillion</td>
<td>£3.2 trillion</td>
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</tbody>
</table>

Particular concerns

- Asset write-downs
- Increasing pension obligations
- Provisions for nuclear decommissioning & clinical negligence
- Vulnerability to future economic shocks

* Accounting deficits in 2009-10 and 2010-11 exclude one-off items.
Five years of improvement, but …

**Significant progress**
- Preparation time from 2 years down to 12 months
- Increased standardisation of accounting across the public sector
- WGA starting to be used to support decision making

**But more to do …**
- Target of 9 months not achieved (v. 3 months in the private sector)
- Finance systems still disjointed and inflexible – just as devolution accelerates
- Lack of comprehensive monthly internal financial reporting

**It’s time …**
- To embed WGA into the financial foundations of Whitehall
- For a modern financial consolidation system – to enable reporting within days not months
Infrastructure funding – a fiscal dilemma

• How to increase infrastructure funding at the same time as sorting the public finances?

• Fiscal charter rule = run a surplus = no new borrowing

• Options:
  – Cut operational spending faster?
  – Bypass the fiscal charter through ‘off balance sheet’ PFI projects?
  – Encourage private sector investment?
  – Investments that pay for themselves?
Flat public investment for next four years

• Government investment plans relatively flat until 2018-19, before an increase in the last year of the parliament

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<tbody>
<tr>
<td>Railways(^a)</td>
<td>7.6</td>
<td>8.2</td>
<td>7.3</td>
<td>7.1</td>
<td>9.8</td>
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<tr>
<td>Schools</td>
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<td>5.1</td>
<td>4.6</td>
<td>4.5</td>
<td>4.5</td>
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<tr>
<td>Highways and roads</td>
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<td>2.8</td>
<td>3.2</td>
<td>3.5</td>
<td>4.0</td>
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<tr>
<td>Housing and regeneration</td>
<td>1.0</td>
<td>1.0</td>
<td>1.3</td>
<td>2.2</td>
<td>2.1</td>
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<tr>
<td>Science</td>
<td>1.1</td>
<td>1.1</td>
<td>1.1</td>
<td>1.2</td>
<td>1.2</td>
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<tr>
<td>Flood defences and other</td>
<td>0.4</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
<td>0.5</td>
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<tr>
<td>Total selected infrastructure</td>
<td>17.5</td>
<td>18.7</td>
<td>18.0</td>
<td>19.1</td>
<td>22.1</td>
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<tr>
<td>Housing associations(^b)</td>
<td>7.9</td>
<td>7.7</td>
<td>7.3</td>
<td>7.2</td>
<td>7.2</td>
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<tr>
<td>Total incl. housing associations</td>
<td>25.4</td>
<td>26.4</td>
<td>25.3</td>
<td>26.3</td>
<td>29.3</td>
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\(^a\) Railways include HS2. \(^b\) Housing association spending estimated by OBR

Source: Autumn Statement 2015 and OBR November 2015.
New PFI projects running at < £2 billion a year

- PFI contracts are now only 2.9% of public sector net debt and neutral to the deficit – is it time to bring them on balance sheet?

Infrastructure investment of £47 billion a year

Source: March 2014 National Infrastructure Investment Pipeline (does not include housing, schools, hospitals or commercial buildings).
Infrastructure funding – the story so far

Less funding from banks
• rebuilding their balance sheets

Less funding from institutional investors
• Monoline insurers – bust, so no AAA bonds anymore

Increased costs
• higher funding costs than before
Government actions

To get better value from PFI
- PF2 contracts – better value for the taxpayer

To provide regulatory or market incentives
- Continued strong investment by price-regulated utilities
- Growing investment in renewables – up until policy changed

Reducing risk for investors
- UK Guarantees to support lending (but only £1.7bn in first two years)

Widening the pool of finance available
- Pensions Infrastructure Platform (but less than £1bn in 4 years)
- Planned collective vehicles for public sector pension funds
Time for a sustainable approach?

**Current approach**
- Off-balance-sheet PFI contracts
- Infrastructure spending within capital budgets

**A commercially sustainable approach**
- Investments with a positive financial return
- Infrastructure spending (including PFI contracts) within capital budgets
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