

Commentary on the Public Sector Finances release: July 2012

1. The Office for National Statistics and HM Treasury published their July 2012 Public Sector Finances bulletin this morning¹. Each month the OBR provides a brief analysis of the data and a comparison with our most recent forecast in the *March Economic and fiscal outlook* (EFO).

Summary

2. The timing of corporation tax payments means that July is usually the second highest month for receipts during the financial year and so typically sees a budget surplus. But this year public sector net borrowing (PSNB) totalled £0.6 billion in July, compared to a surplus of £2.8 billion last year.
3. This reflects both a drop in central government receipts and strong central government spending. The 0.8 per cent decline in receipts from a year ago is primarily due to a sharp fall in corporation tax receipts, in particular from the oil and gas sector. This largely reflects weaker-than-expected production.
4. Excluding the impact of moving the Royal Mail's historic pension fund deficit and associated assets into the public sector, the *March Economic and fiscal outlook* (EFO) forecast a £5.1 billion improvement in PSNB in 2012-13 compared to 2011-12. But after the first four months of the financial year, PSNB (excluding Royal Mail) is £9.3 billion higher than last year:
 - central government current expenditure growth of 3.5 per cent in the first four months of 2012-13 compares to a full year forecast in the March EFO of 3.1 per cent. However, expenditure data is volatile on a monthly basis and is often revised;
 - growth in central government receipts of 1.1 per cent in the first four months of the financial year is well below the full year forecast in the March EFO of 3.9 per cent. Corporation tax receipts have been weaker than expected. Firms make instalment payments based on their expectations of full year profits, so the instalment payments due in October 2012 and January 2013 are also likely to be lower than forecast in the EFO. In contrast, national insurance contributions, the PAYE element of income tax and VAT are much closer to their full year forecasts; and

¹ <http://www.ons.gov.uk/ons/rel/psa/public-sector-finances/july-2012/stb---july-2012.html>

- at this relatively early stage of the financial year, there is very significant uncertainty around the local authority and public corporations borrowing figures. These are prone to substantial revisions.
5. Overall, there continues to be significant uncertainty around the prospects for full year borrowing. While it looks likely that corporation tax receipts will fall short of our March *EFO* forecast, the other main receipts streams remain closer to forecast. Clearly much will depend on the performance of the real economy and inflation over the remainder of the fiscal year. It is too early to judge whether full year central government expenditure will overshoot the *EFO* forecast.

July 2012 outturn

6. Borrowing of £0.6 billion in July 2012 is only the third time in fifteen years that a surplus has not been recorded in July. Compared to last year, the swing into deficit this July mainly reflects a £0.4 billion drop in receipts and a £3.1 billion rise in central government spending.
7. July is an important month for receipts since many firms pay the first corporation tax instalment payment on their 2012 profits during the month. The second payment on account for self assessment (SA) liabilities for 2011-12 was also due on July 31. SA receipts were up over 20 per cent in July on a year earlier. With the due date at the end of the month, payments will be collected in both July and August. So some of the strength in July relative to last year could be a timing effect and may therefore unwind in August. Despite the strength of SA receipts, central government receipts fell by 0.8 per cent on a year earlier, reflecting a 20 per cent drop in corporation tax receipts.
8. Corporation tax receipts from oil and gas producers were particularly weak. The March *EFO* forecast had anticipated some fall in such receipts compared to 2011 - the effect on receipts from modestly higher oil and gas prices was expected to be offset by lower oil production and higher capital expenditure. However, combined oil and gas production has fallen by 15 per cent in the first half of 2012 from a year earlier. This compares with the DECC projections of flat gas production and a 7 per cent fall in oil production that were included in the *EFO* forecast (based on survey data from operators). Production in the first half of 2012 was particularly affected by the Elgin gas leak. Indications are that production in the second half of 2012 will be reduced by unusually high levels of maintenance in the North Sea.
9. Oil prices averaged \$114 a barrel in the first half of 2012, only a little below the \$118 a barrel assumed for 2012 as a whole in the March *EFO*. However, the July payments could have been influenced by the drop below \$100 a barrel just prior to the payment date.
10. Corporation tax receipts from industrial and commercial companies also showed a fall on a year earlier. The ONS have yet to publish an income breakdown of second quarter GDP, but the outturns for non-oil, non-financial profits in the final quarter of 2011 and the first quarter of 2012 showed year-on-year falls, weaker than assumed

in the March EFO forecast. It is possible that the combination of the fall in GDP allied with strong rises in employment has had the effect of squeezing profits.

11. Central government current expenditure increased by 5.1 per cent in July. Spending data has been volatile on a monthly basis so far in 2012-13. The latest central government spending data show that:
 - debt interest payments in July were down by almost 19 per cent on levels seen in July 2011. This reflects the monthly RPI profile compared with a year earlier, which affects debt interest on index-linked gilts;
 - net social benefit payments in July were 6.2 per cent higher than in the same period last year, compared to our March EFO forecast of a 5.8 per cent full year increase;
 - other current spending (primarily spending on public services) increased by 7.9 per cent in July compared with July 2011. This was partly driven by larger payments of grants to local authorities in July compared to last year; and
 - net investment was up by 32.8 per cent in July compared to a year earlier. Monthly investment spending is very volatile and the data are prone to revision and so there are no clear trends emerging yet.

Outturn for April to July 2012

12. Revisions in this month's release to the data for the first three months of 2012-13 have raised PSNB by £1.4 billion. This is primarily due to an upward revision of nearly £1.5 billion in central government spending.
13. Central government receipts growth of 1.1 per cent for the first four months of the financial year was well below the 3.9 per cent required to meet the March EFO forecast for 2012-13 as a whole. Corporation tax is clearly weaker than the full year forecast and given that firms should make instalment payments based on their views of full year profits, it is likely that subsequent instalment payments will be weaker than anticipated as well.
14. Growth in other key receipts streams are much closer to their full year forecasts from the March EFO. National insurance contributions are growing more strongly than their full year forecast, while growth in accrued VAT receipts are also a little above. In addition, the PAYE element of income tax is growing in line with the full year forecast. Other elements of income tax are weaker relative to the full year EFO forecast, but this in large part reflects the change in the timing of non-SA repayments compared with last year.
15. Central government current expenditure grew by 3.5 per cent for the first four months of the financial year, a little above the 3.1 per cent assumed in the March EFO forecast. Both debt interest and net social benefits have grown more strongly than assumed in March. With RPI inflation falling, we expect the year-to-date growth in debt interest payments compared to the same period last year to fall further over

the remainder of 2012-13. Growth in net social benefits has been volatile because of timing differences with the profile of payments last year. So it is likely to take more time before any trends become clear.

Issues for next PSF release: August 2012

16. The August figures will include the ticketing income and some spending from the Olympic Games. This will affect the net borrowing of public corporations, although the overall effect is likely to be relatively small. While August is a quiet month for receipts, the release will provide an extra month of data to assess the March EFO forecast.

Public sector receipts, expenditure and net borrowing

| £ billion | July | | | | April to July | | | | Implied August to March | | | | Full Year | | | |
|---|-------------|-------------|-------------|--------------|---------------|--------------|--------------|--------------|-------------------------|--------------|--------------|--------------|---------------------|--------------------|--------------|---------------|
| | 2012 | 2011 | change | | 2012-13 | 2011 -12 | change | | 2012-13 | 2011-12 | change | | 2012-13 Mar EFO* | 2011-12 outturn | change | |
| | | | £bn | % | | | £bn | % | | | £bn | % | | | £bn | % |
| Central Government (CG) current receipts | | | | | | | | | | | | | | | | |
| Taxes on production | 18.0 | 17.0 | 1.0 | 5.7 | 68.2 | 66.1 | 2.2 | 3.3 | 145.8 | 135.9 | 9.9 | 7.3 | 214.0 | 202.0 | 12.0 | 6.0 |
| <i>Of which: VAT (accrued)</i> | 9.7 | 9.1 | 0.6 | 6.3 | 37.9 | 36.2 | 1.8 | 4.8 | 76.7 | 73.5 | 3.2 | 4.3 | 114.6 | 109.7 | 4.9 | 4.4 |
| Taxes on income and wealth | 23.3 | 24.9 | -1.5 | -6.1 | 61.6 | 63.6 | -2.0 | -3.1 | 139.6 | 134.0 | 5.6 | 4.2 | 201.2 | 197.6 | 3.6 | 1.8 |
| <i>Of which:</i> | | | | | | | | | | | | | | | | |
| <i>Income tax and CGT (accrued)</i> | 16.2 | 16.1 | 0.2 | 1.1 | 46.6 | 46.8 | -0.2 | -0.5 | 107.8 | 105.0 | 2.8 | 2.7 | 154.4 | 151.8 | 2.6 | 1.7 |
| <i>Corporation tax</i> | 6.9 | 8.6 | -1.7 | -20.3 | 14.1 | 15.9 | -1.8 | -11.3 | 29.7 | 26.2 | 3.5 | 13.2 | 43.8 | 42.2 | 1.7 | 4.0 |
| Other taxes | 1.4 | 1.7 | -0.3 | -17.7 | 5.1 | 5.0 | 0.1 | 2.0 | 10.6 | 10.3 | 0.3 | 3.4 | 15.7 | 15.3 | 0.4 | 2.9 |
| Compulsory social contributions | 8.7 | 8.3 | 0.3 | 4.2 | 34.4 | 32.9 | 1.5 | 4.4 | 71.2 | 69.1 | 2.1 | 3.0 | 105.6 | 102.0 | 3.6 | 3.5 |
| Interest & dividends | 0.5 | 0.4 | 0.1 | 35.4 | 2.1 | 1.7 | 0.4 | 20.4 | 5.5 | 5.6 | -0.1 | -1.8 | 7.6 | 7.3 | 0.3 | 4.1 |
| Other receipts | 0.6 | 0.7 | 0.0 | -7.1 | 2.5 | 2.7 | -0.2 | -7.2 | 6.1 | 5.2 | 0.9 | 17.2 | 8.6 | 7.9 | 0.7 | 8.8 |
| Total CG current receipts | 52.5 | 52.9 | -0.4 | -0.8 | 173.9 | 172.0 | 1.9 | 1.1 | 378.7 | 360.0 | 18.7 | 5.2 | 552.6 | 532.0 | 20.6 | 3.9 |
| CG Current expenditure | | | | | | | | | | | | | | | | |
| Interest payments | 3.3 | 4.1 | -0.8 | -18.9 | 17.4 | 17.6 | -0.1 | -0.8 | 27.4 | 29.6 | -2.2 | -7.4 | 44.8 | 47.2 | -2.4 | -5.0 |
| Net social benefits | 16.0 | 15.0 | 0.9 | 6.2 | 63.5 | 59.3 | 4.2 | 7.0 | 128.4 | 122.0 | 6.4 | 5.2 | 191.9 | 181.3 | 10.6 | 5.8 |
| Other | 31.0 | 28.7 | 2.3 | 7.9 | 131.7 | 128.4 | 3.2 | 2.5 | 267.5 | 260.1 | 7.4 | 2.9 | 399.2 | 388.5 | 10.7 | 2.8 |
| Total current expenditure | 50.2 | 47.8 | 2.4 | 5.1 | 212.5 | 205.3 | 7.3 | 3.5 | 423.4 | 411.7 | 11.7 | 2.8 | 635.9 | 617.0 | 18.9 | 3.1 |
| Depreciation | 0.7 | 0.6 | 0.1 | 9.1 | 2.7 | 2.5 | 0.2 | 7.9 | 5.2 | 5.0 | 0.2 | 4.3 | 7.9 | 7.5 | 0.4 | 5.5 |
| CG Surplus on current budget | 1.6 | 4.5 | -2.9 | -65.2 | -41.3 | -35.8 | -5.6 | -15.5 | -49.9 | -56.7 | 6.8 | -12.0 | -91.2 | -92.5 | 1.3 | -1.4 |
| CG Net investment | 2.5 | 1.9 | 0.6 | 32.8 | -21.2 | 7.6 | -28.8 | | 21.9 | 15.0 | 6.9 | 46.4 | 0.7 | 22.6 | -21.9 | -96.9 |
| CG Net borrowing | 1.0 | -2.5 | 3.5 | 138.6 | 20.1 | 43.4 | -23.2 | -53.6 | 71.8 | 71.6 | 0.2 | 0.3 | 91.9 | 115.0 | -23.1 | -20.1 |
| Local Authorities net borrowing | -0.7 | -0.6 | -0.1 | -21.5 | -4.3 | -7.6 | 3.4 | 44.0 | 4.9 | 18.4 | -13.5 | -73.4 | 0.6 | 10.8 | -10.2 | -94.5 |
| Public Corporations net borrowing | 0.3 | 0.3 | 0.0 | -2.5 | 1.1 | -0.2 | 1.2 | | -1.7 | -0.7 | -1.0 | 147.5 | -0.6 | -0.9 | 0.3 | -32.9 |
| Public sector net borrowing | 0.6 | -2.8 | 3.4 | 119.6 | 16.9 | 35.6 | -18.7 | -52.4 | 75.0 | 89.4 | -14.4 | -16.1 | 91.9 | 125.0 | -33.1 | -26.5 |
| PSNB (ex Royal Mail) | 0.6 | -2.8 | 3.4 | 119.6 | 44.9 | 35.6 | 9.3 | 26.2 | 75.0 | 89.4 | -14.4 | -16.1 | 119.9 | 125.0 | -5.1 | -4.1 |
| Public sector net investment | 1.7 | 1.4 | 0.4 | 27.5 | -25.1 | 4.7 | -29.9 | | 21.7 | 21.4 | 0.3 | 1.5 | -3.4 | 26.1 | -29.5 | -113.0 |
| Public sector current budget | 1.2 | 4.2 | -3.0 | -71.8 | -42.1 | -30.9 | -11.2 | -36.3 | -53.2 | -68.0 | 14.8 | -21.8 | -95.3 | -98.9 | 3.6 | -3.6 |

March 2012 EFO forecast published 21 March 2012 excluding temporary effects of financial interventions on a National Accounts basis