

Commentary on the Public Sector Finances: May 2019

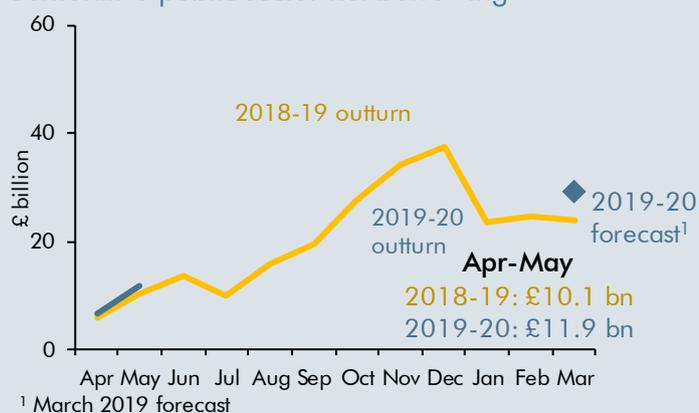
Office for
**Budget
Responsibility**

21 June 2019

Student loans to add £10 billion to measured deficit

Public sector borrowing was higher than last year, both in May and over the year to date. More materially, a forthcoming improvement in the accounting treatment of student loans will raise the measured deficit by more than £10 billion a year. This is close to our estimate from March, when we thought it would reduce headroom against the fiscal mandate by around 40 per cent.

Cumulative public sector net borrowing



Headlines

- **Public sector net borrowing (PSNB)** in May was £5.1 billion, £1.0 billion up on last year.
- **We expect a small rise in borrowing in 2019-20.** This reflects the income tax giveaways announced in Budget 2018 and higher departmental spending (on the NHS in particular).
- **Central government receipts** (excluding PSNB-neutral transfers related to 'quantitative easing') were up 3.5 per cent in May and for the year-to-date, above our full-year forecast of a 2.7 per cent rise (on a like-for-like basis).
- **Central government spending** (excluding PSNB-neutral grants to local authorities) was up 5.3 per cent in May and 5.0 per cent for the year-to-date, above our full-year forecast of a 3.3 per cent rise (on a like-for-like basis).
- **Net debt** was 1.4 per cent of GDP lower in May 2019 than it was in May 2018.
- **PSNB for 2018-19** was revised up by £0.5 billion to £24.0 billion, and is now £1.2 billion above our March forecast.
- The ONS presented indicative estimates of the effect of **the new accounting treatment for student loans**, which it intends to incorporate fully in its September release. This adds materially to measured borrowing – by £10.6 billion in 2018-19. This is consistent with the estimate from our March forecast. The effect will rise year by year in the medium term.

Full commentary

1. The Office for National Statistics and HM Treasury published their Statistical Bulletin on the May 2019 Public Sector Finances this morning.¹ Each month the OBR provides a brief analysis of the data and a comparison with our most recent forecast, currently the March 2019 *Economic and fiscal outlook (EFO)*.
2. The headline statistics continue to reflect the existing treatment of student loans in public sector net borrowing, but the ONS has published indicative estimates of the effect of the forthcoming changes that will be implemented in full in September. These will remove the most problematic ‘fiscal illusions’ generated by the existing treatment and will add more than £10 billion a year to the measured deficit. The indicative estimates are described at the end of this commentary. The fiscal illusions generated under the current treatment were described in a working paper we published last year.²

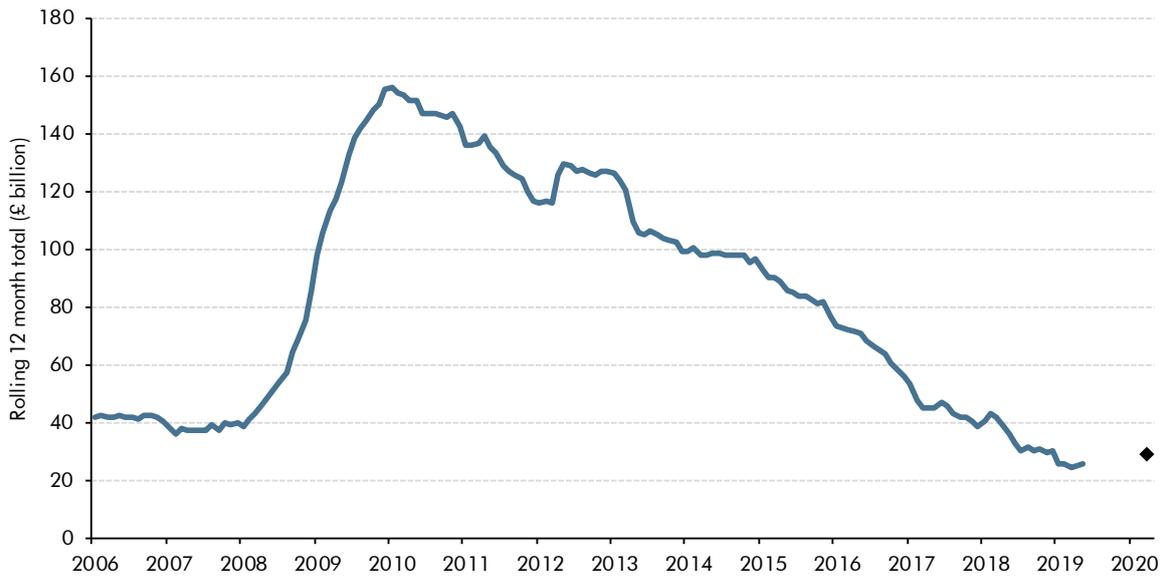
Public sector net borrowing

3. Public sector net borrowing (PSNB) was £5.1 billion in May, around £1.0 billion higher than last year and £1.0 billion above market expectations. A £1.9 billion (3.5 per cent) rise in central government (CG) receipts was more than offset by a £2.5 billion (4.2 per cent) rise in CG spending. Borrowing by local authorities was £0.4 billion higher than last year, while the surplus from public corporations was unchanged from last year.
4. Chart 1.1 shows outturn PSNB on a 12-month rolling basis, relative to our latest full-year forecast for 2019-20. We expect a small rise in borrowing in 2019-20, only partly reversing the large fall in 2018-19. This reflects a forecast of slower growth in receipts reflecting the Budget 2018 announcements on the income tax personal allowance and higher rate threshold, the temporary rise in the annual investment allowance to £1 million, and slower growth in the main nominal tax bases in 2019. CG spending is expected to be stronger, particularly DEL spending on public services thanks to the additional resources for the NHS announced in June 2018.

¹<https://www.ons.gov.uk/economy/governmentpublicsectorandtaxes/publicsectorfinance/bulletins/publicsectorfinances/may2019>

² OBR Working Paper No. 12: ‘Student Loans and Fiscal Illusions’, Jim Ebdon and Reece Waite, July 2018

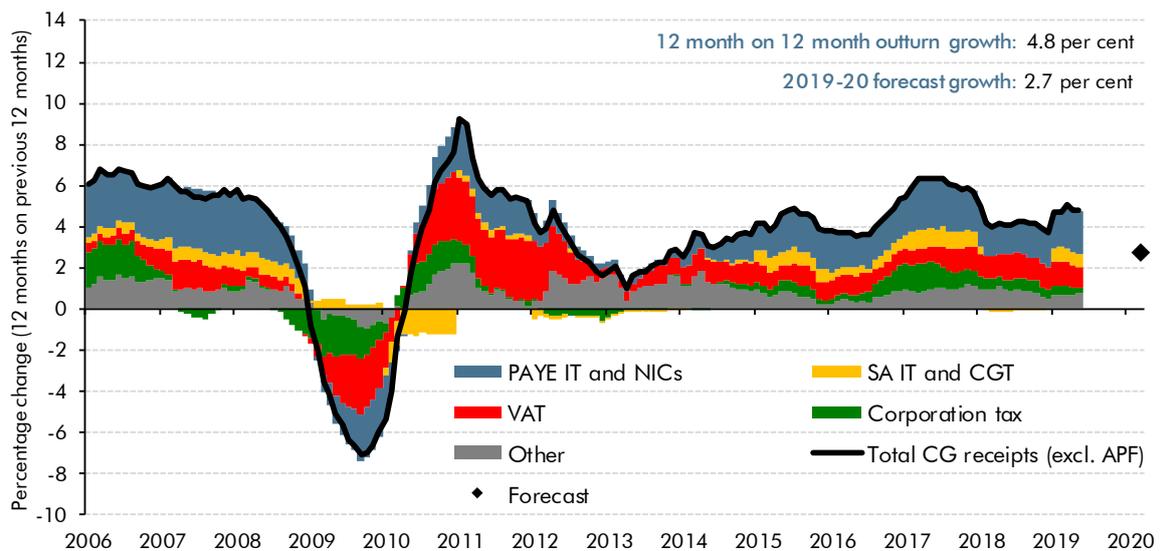
Chart 1.1: Public sector net borrowing: rolling 12-month total



Source: ONS, OBR

- Relative to last year, CG receipts (excluding APF transfers) were up 3.5 per cent in May and for the year-to-date, above the 2.7 per cent rise we expect for the whole of 2019-20 (on a like-for-like basis). Receipts growth in May mainly reflected rises in PAYE income tax, National Insurance contributions and VAT. Year-to-date receipts growth has also benefited from the £0.8 billion special dividend received on the Government’s RBS shares that scored in April. Chart 1.2 shows the rolling 12-month average growth in CG receipts. We would expect this to slow as 2019-20 progresses.

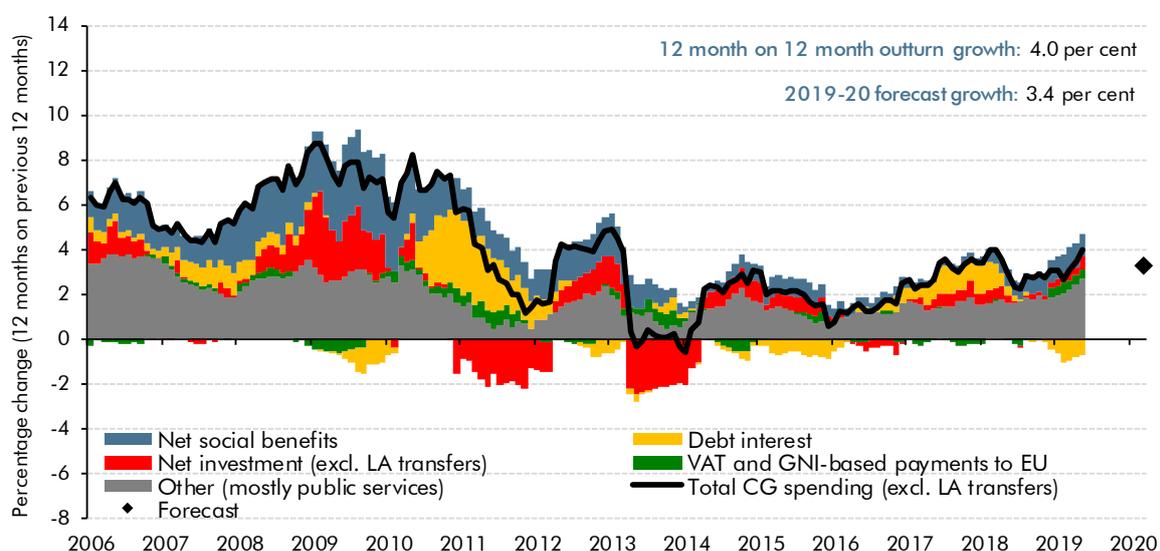
Chart 1.2: Growth in central government receipts: rolling 12-month average



We have adjusted these figures for differences between our forecasts and ONS outturns that stem from classification decisions the ONS has taken but not yet implemented. Full details are available in a supplementary table on our website.
Source: ONS, OBR

6. Relative to last year, total CG spending (excluding grants to local authorities) was up 5.3 per cent in May and up 5.0 per cent for the year to date (following upward revisions to April data). That is above our full-year forecast for 2019-20 of 3.3 per cent growth (on a like-for-like basis), although spending data this early in the financial year are very provisional (and often based on departmental forecasts) and subject to revision. Departmental current and capital spending has shown the strongest growth. For April and May combined, other CG current expenditure (largely spending on public services) was up 8.6 per cent on a year earlier, boosted by the more generous NHS settlement, while CG net investment was up 10.3 per cent on last year. Chart 1.3 shows CG spending growth on a 12-month rolling basis.

Chart 1.3: Growth in central government spending: rolling 12-month average



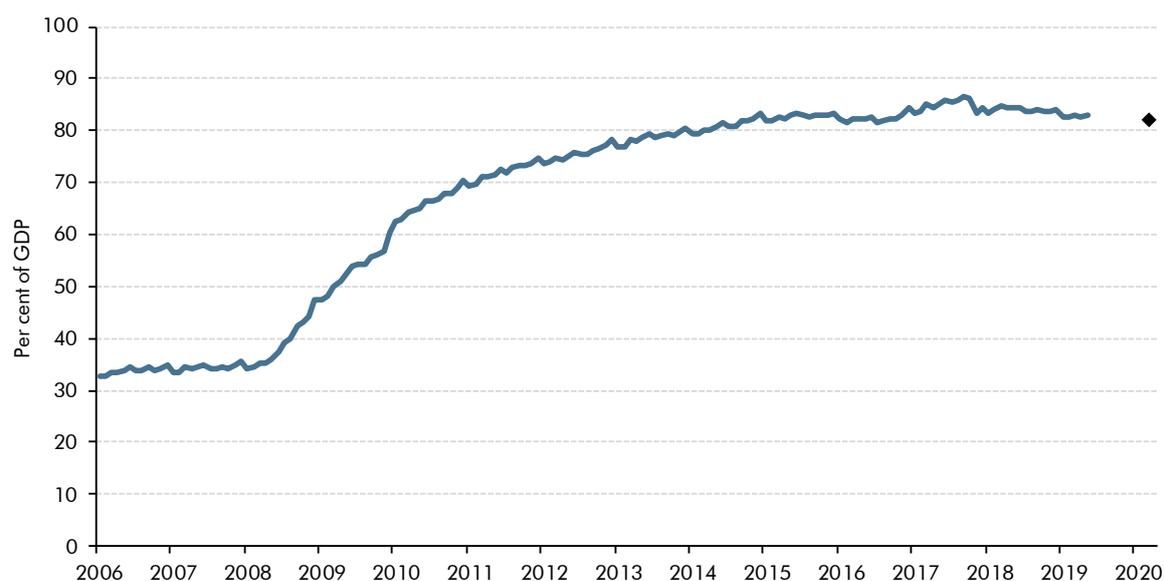
We have adjusted these figures for differences between our forecasts and ONS outturns that stem from classification decisions the ONS has taken but not yet implemented. Full details are available in a supplementary table on our website.

Source: ONS, OBR

Debt

7. Public sector net debt (PSND) in May 2019 was down 1.4 per cent of GDP from a year earlier. The year-on-year drop is partly explained by the £4.9 billion sale of Bradford and Bingley mortgages by UK Asset Resolution (UKAR) in April and a £4 billion early repayment of Term Funding Scheme (TFS) loans in May. The UKAR sale was part of the £16.4 billion of financial asset sales expected during 2019-20 in our March forecast, but we did not assume that any further TFS loans would be repaid early.

Chart 1.4: Public sector net debt



Source: ONS, OBR

Provisional 2018-19 estimate

8. The provisional estimate for PSNB for 2018-19 has been revised up by £0.5 billion. It is now £1.2 billion above our March forecast. Abstracting from some items that are not yet in the ONS outturns (which would lower the difference with our March forecast to £0.9 billion), CG spending was £1.8 billion higher than expected and borrowing by public corporations £1.6 billion higher. This was partly offset by £0.4 billion higher CG receipts and £2.1 billion lower borrowing by local authorities. Further revisions in the coming months can be expected as full outturns become available.

Student loans accounting treatment change

9. The ONS has released provisional estimates of the impact of forthcoming changes to the accounting treatment of student loans. These split loan outlays into a portion that is treated as a conventional loan, which generates an associated asset and does not score against the deficit, and a portion that is treated as spending, which does affect the deficit. At the moment, all outlays are treated as loans despite the fact that a significant proportion are expected to be written off rather than repaid.
10. The ONS estimates the impact on the deficit in 2018-19 as an increase of £10.6 billion, close to the £10.5 billion we estimated in our March 2019 forecast. The effect has been on a rapidly rising path, with the ONS estimating that it stood at £3.7 billion five years ago and just £0.9 billion a decade ago. The accompanying ONS article indicates that most of the methodological development work has been completed, so the degree of uncertainty around these estimates has diminished relative to those we have presented in recent *EFOs*. The new methodology will be incorporated into the public finance statistics in September and we will reflect that change in our next fiscal forecast.

Table 1.1: Public sector receipts, expenditure and net borrowing¹

£ billion	May				April to May				June to March				2019-20 EFO	March forecast			
	2019	2018	change		2019-20	2018-19	change		2019-20	2018-19	change			2019-20	2018-19	change	
			£bn	%			£bn	%			£bn	%				£bn	%
Central government (CG) current receipts																	
Taxes on production	23.1	22.4	0.6	2.9	46.6	45.9	0.7	1.5	241.8	232.6	9.2	4.0	288.4	278.5	9.9	3.6	
Of which: VAT (accrued)	12.6	12.1	0.5	4.4	25.5	24.5	1.0	3.9	129.5	126.4	3.2	2.5	155.0	150.9	4.1	2.7	
Taxes on income and wealth ¹	17.9	17.4	0.5	3.0	36.2	35.3	0.9	2.4	229.1	226.5	2.7	1.2	265.3	261.8	3.5	1.3	
Of which:																	
Income tax and CGT (accrued)	12.6	12.0	0.6	4.9	25.7	24.9	0.8	3.2	179.1	176.6	2.5	1.4	204.8	201.5	3.3	1.6	
Corporation tax (accrued)	5.2	5.3	0.0	-0.8	10.5	10.4	0.1	0.6	49.7	49.9	-0.2	-0.4	60.2	60.3	-0.1	-0.2	
Other taxes	1.5	1.6	-0.1	-5.5	3.1	3.1	0.0	0.4	15.3	15.3	0.0	0.0	18.3	18.3	0.0	0.1	
Compulsory social contributions	11.3	10.6	0.7	6.5	22.8	21.6	1.2	5.6	120.6	116.1	4.5	3.8	143.4	137.7	5.7	4.1	
Interest & dividends	0.9	0.9	0.0	5.0	5.6	5.1	0.5	8.9	16.5	15.7	0.8	4.9	22.1	20.9	1.2	5.9	
Other receipts	2.0	1.9	0.1	6.0	4.0	3.8	0.3	7.0	20.2	19.5	0.8	3.9	24.3	23.3	1.0	4.4	
Total CG current receipts	56.7	54.8	1.9	3.5	118.4	114.9	3.5	3.0	643.5	625.6	17.9	2.9	761.8	740.5	21.4	2.9	
CG current expenditure																	
Interest payments	3.1	3.5	-0.3	-8.9	9.4	9.6	-0.3	-2.7	41.7	39.0	2.7	6.9	51.1	48.7	2.4	5.0	
Net social benefits	18.3	18.1	0.1	0.8	36.5	35.8	0.8	2.2	174.9	179.0	-4.1	-2.3	211.4	214.7	-3.3	-1.5	
CG current grants to LAs	9.0	9.3	-0.3	-3.5	20.1	20.3	-0.2	-1.1	94.1	92.7	1.5	1.6	114.3	113.0	1.2	1.1	
VAT and GNI-based payments to EU ²	0.6	0.8	-0.1	-16.1	1.4	1.7	-0.4	-20.4	11.5	11.2	0.4	3.2	12.9	12.9	0.0	0.0	
Other CG current expenditure	26.5	24.4	2.1	8.5	53.8	49.5	4.3	8.6	271.9	258.0	13.9	5.4	325.7	307.5	18.1	5.9	
Total current expenditure	57.5	56.1	1.5	2.6	121.2	117.0	4.2	3.6	594.2	579.9	14.3	2.5	715.3	696.9	18.5	2.7	
Depreciation	1.6	1.5	0.0	2.8	3.2	3.1	0.1	2.8	16.0	15.5	0.5	3.1	19.1	18.6	0.6	3.1	
CG current budget deficit	2.4	2.8	-0.4	-14.5	6.0	5.2	0.8		-33.4	-30.2	-3.1	10.3	-27.4	-25.1	-2.3		
CG net investment	3.5	2.4	1.0	41.1	7.0	6.3	0.7	10.3	42.7	38.1	4.6	12.1	49.7	44.4	5.3	11.8	
of which: CG capital grants to LA	1.2	1.0	0.2	19.9	2.8	2.8	0.1	2.0	8.8	8.9	-0.1	-1.1	11.6	11.6	0.0	-0.4	
CG net borrowing	5.9	5.3	0.6		12.9	11.5	1.5	12.6	9.4	7.9	1.5		22.3	19.4	2.9	15.2	
Local authorities net borrowing	0.2	-0.2	0.4		-2.2	-2.8	0.6	-22.4	11.4	8.9	2.5	28.2	9.3	6.1	3.2	51.4	
Public corporations net borrowing	-0.9	-0.9	0.0		1.1	1.4	-0.3	-19.7	-3.4	-2.9	-0.5		-2.3	-1.5	-0.8	51.9	
Public sector net borrowing	5.1	4.2	1.0	23.1	11.9	10.1	1.8	17.8	17.4	13.9	3.5	25.4	29.3	24.0	5.3	22.2	
Public sector net investment	2.1	1.6	0.6	36.6	3.9	3.8	0.2	4.9	43.1	37.9	5.2	13.7	47.0	41.7	5.4	12.9	
Public sector current budget	3.0	2.6	0.4	15.0	8.0	6.4	1.6	25.4	-25.7	-24.0	-1.7		-17.7	-17.6	0.0		

March 2019 EFO forecast published 13 March 2019 excluding public sector banks on a National Accounts basis.

¹ Data and forecasts contained in this table can be found from the following sources:

ONS public sector finances: <https://www.ons.gov.uk/economy/governmentpublicsectorandtaxes/publicsectorfinance/bulletins/publicsectorfinances/may2019>

HMRC tax receipts and national insurance contributions: <https://www.gov.uk/government/statistics/hmrc-tax-and-nics-receipts-for-the-uk>

OBR Economic and fiscal outlook: https://cdn.ubr.uk/EFO_March-2019.pdf

² Net of abatement.