Office for
Budget Responsibility

23 September 2014

Commentary on the Public Sector Finances release: August 2014

1. The Office for National Statistics and HM Treasury published their Statistical Bulletin on the August 2014 Public Sector Finances this morning.[1] This is the first release in which the public finances data are presented on the basis of new methodologies that reflect the updated 2010 European System of Accounts (ESA10) and the conclusions of the ONS review of the public finances statistics.

2. The headline measure of the deficit is now 'public sector net borrowing excluding public sector banks' – which removes the effect of the public sector banks from overall borrowing – rather than 'public sector net borrowing excluding financial interventions' – which also excluded the effects of other unusual operations deemed to result from the financial crisis such as the Special Liquidity Scheme, though not the cash transfers to the Exchequer from the Asset Purchase Facility (APF) related to quantitative easing. The main changes and their illustrative effects on our forecasts were described in Annex B of our March 2014 *Economic and fiscal outlook (EFO)*. As we noted at the time, it is important to stress that these are changes to the way the public sector's finances are measured, not to the underlying activities being measured.

3. The changes implemented in today's release mean the detailed public finances data are no longer presented on a basis that is consistent with our March 2014 *EFO*, which were consistent with the 1995 European System of Accounts (ESA95). This makes it more difficult to draw inferences from the latest data for performance against our latest forecast. Our forthcoming December 2014 *EFO* will present forecasts on the new basis. In the intervening period, our monthly commentary will focus on year-on-year developments in the outturn data and a high level summary of where meaningful messages can be drawn on performance against forecast. (We have also suspended the detailed table comparing outturn data and forecast, which will be reinstated after the December 2014 *EFO*.)

Outturns on the new basis for August 2014 and for the fiscal year to date

4. Public sector net borrowing (PSNB) was £11.6 billion in August, £0.2 billion lower than market expectations and £0.7 billion higher than a year ago. Central government spending was £1.7 billion up on last year, while central government

[1] http://www.ons.gov.uk/ons/rel/psa/public-sector-finances/august-2014/stb---august-2014.html

receipts were up by only £1.4 billion. Borrowing by local authorities and public corporations was also £0.3 billion higher than last year.

5. For the first five months of 2014-15, PSNB was £45.4 billion, £2.6 billion higher than a year ago.

Performance against forecast

6. The changes to the public finances data make it difficult to draw inferences about performance against our latest forecast. In Annex B of our March *EFO* we provided illustrative forecasts on the new basis, consistent with our understanding at the time of the forthcoming revisions. The ONS has provided a detailed reconciliation of the changes to the main fiscal aggregates in today's release – Table 1 summarises these effects for the main measures of borrowing and debt.[2]

7. Until we produce a full set of forecasts on the new basis in December, perhaps the best way to consider performance against forecast is to look at year-on-year changes in those elements of the public finances that are either little affected by the revisions or are unlikely to be affected by different amounts from year to year. That means, for example, that it will be particularly difficult to compare net investment against our forecast until December, because we will need to forecast the Network Rail investment that is now included in the public finances data, and the ONS data show that this investment varies from year to year.

8. With these caveats in mind, the main conclusions to draw from the latest public finances data are that:

   - PSNB has risen by 6.2 per cent in the year-to-date, whereas we were expecting a fall for 2014-15 as a whole in our March forecast;

   - receipts have grown by just 2.0 per cent so far this year, compared with our forecast of close to 5 per cent for the full year, excluding receipts from the APF. In particular, income tax receipts have fallen by 0.8 per cent against a full year forecast of a 6.5 per cent rise. Some of this reflects the timing of receipts growth through the financial year. Last year's shifting of PAYE liabilities in response to the reduction in the additional rate of income tax depressed receipts growth in the early part of 2014-15. We also expect a sizeable boost to SA receipts at the end of January 2015 when the balancing payment for 2013-14 liabilities is made, again reflecting the shifting of liabilities related to the additional rate. That said, weaker-than-expected wage growth so far in 2014-15 also appears to be depressing PAYE and NIC receipts. Unexpectedly weak earnings growth and strong employment growth also mean that a greater proportion of wages and salaries will be subject to the £10,000 personal allowance, reducing the effective tax rate on labour income.

[2] ONS's comprehensive revisions analysis can be found at http://www.ons.gov.uk/ons/rel/psa/public-sector-finances/august-2014/rft---revisions-table.xls
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- growth in stamp duty land tax receipts, while strong at 23.8 per cent year-on-year in August, is a little lower than our full-year forecast of 35 per cent. This may be because the Mortgage Market Review is depressing property transactions by more than we anticipated. In contrast, VAT receipts have grown by 4.6 per cent since last year so far in 2014-15, compared with a full year forecast of 4.2 per cent. Today's methodological revisions should have little effect on these comparisons; and

- central government current spending has grown by 1.3 per cent since last year so far in 2014-15, compared with our full-year forecast of 1.9 per cent. However this comparison will be affected by today's upward revisions to 2013-14 spending. As we explained last month, lower payments of debt interest and current grants to local authorities have reduced spending over the first five months of the year, but we expect most of the timing differences on grants to local authorities to unwind over the rest of the year.

Methodological revisions

9. Table 1 summarises the methodological revisions in today's release, which change the data onto the new ESA10 basis, and implement the recommendations from the PSF review. The key points to note are that:

   - the new public sector net borrowing (excluding public sector banks) measure is higher by £5.6 billion in 2013-14 than the previous PSNB (excluding financial interventions) measure, of which £3.6 billion is due to the methodological revisions. This reflects the inclusion of borrowing by Network Rail and imputed contributions to local government pension schemes, which both raise borrowing. The 2012 transfer of the Royal Mail Pension plan is also being treated differently. It now increases rather than reduces borrowing in 2012-13, but reduces borrowing slightly thereafter. The proceeds from the 3G and 4G spectrum auctions in 2000-01 and 2012-13 are also now treated as flows of rent over a number of years rather than one-off negative capital spending (increasing the deficit in the auction years relative to the previous treatment and reducing it thereafter); and

   - public sector net debt in 2013-14 is higher by £129 billion in cash terms. This is because the debt of Network Rail and the APF are now being included in the measure and that bank shares bought by the government during the financial crisis are now treated as an illiquid asset rather than a liquid one (so that they no longer reduce the headline measure of net debt).

Table 1: Methodological revisions to public sector borrowing and debt

	Previous treatment [1]			Latest treatment			Methodological revisions		Difference in
	2012-13	2013-14	Percentage	2012-13	2013-14	Percentage	2012-13	2013-14	percentage
	£ billion	£ billion	growth	£ billion	£ billion	growth	£ billion	£ billion	growth
Total public sector, excluding banks									
Current receipts (PSCR)	594.7	621.4	4.5%	598.5	622.4	4.0%	3.8	1.0	-0.5%
Current spending (PSCE)	656.8	668.9	1.8%	648.1	659.5	1.8%	-8.7	-9.4	-0.1%
Depreciation	25.4	26.5	4.2%	34.3	36.1	5.2%	8.9	9.6	0.9%
Current budget deficit	**87.5**	**74.0**	-15.4%	**84.0**	**73.2**	-12.9%	**-3.5**	**-0.8**	2.6%
Net investment (PSNI)	-7.1	21.6	-	35.4	26.1	-26.4%	42.5	4.5	-
PSNB	**80.5**	**95.7**	**18.8%**	**119.4**	**99.3**	**-16.9%**	**38.9**	**3.6**	**-35.7%**
PSND [2]	**1,186**	**1,274**	**7.4%**	**1,299**	**1,402**	**7.9%**	**113**	**129**	**0.5%**

[1] Derived from the latest data, excluding the revisions to change the data onto the new ESA10 basis, and to implement the PSF review. Definitions under previous treatment exclude the temporary effects of financial interventions.

[2] Methodological revisions for PSND derived as total revisions, excluding 'other' data revisions for changes other than ESA 10 and implementation of PSF review.

Other revisions to 2013-14 outturn

10. Separately, and in addition to all definitional changes that the ONS has made to the outturn data for ESA10 and their review of the public finances statistics, the ONS has also revised the 2013-14 outturn data to reflect the new information on 2013-14 outturns. These latest changes have revised up the estimate for PSNB for 2013-14 by a further £2.0 billion.

11. This mainly reflects an upward revision of £2.1 billion to central government current spending to reflect departments' provisional outturn data (as published in Public Expenditure Statistical Analyses 2014). These revisions do not yet include the provisional outturn data for local authority current expenditure that were released at the end of August – we expect that these latest data will be included in next month's Public Sector Finances release.

12. Our 2014 *Forecast evaluation report,* which we will publish on 16 October, will contain further details of our analysis of the latest outturn data for 2013-14.