
INTRODUCTION

The Budget 2005 projections for the public finances are broadly in line with the 2004 Pre-Budget Report and show that the Government is meeting its strict fiscal rules:

- the current budget shows an average surplus of 0.1 per cent of GDP over the current economic cycle, even using cautious assumptions, ensuring the Government is meeting the golden rule. The average current surplus from 2005-06 to the end of the forecast period is 0.3 per cent of GDP; and
- public sector net debt is projected to remain low and stable over the forecast period, stabilising at 37 per cent of GDP, well below the 40 per cent ceiling in the sustainable investment rule.

C1 Chapter 2 describes the Government's fiscal policy framework and shows how the projections of the public finances are consistent with meeting the fiscal rules. This chapter explains the latest outturns and the fiscal projections in more detail. It includes:

- five-year projections of the current budget and public sector net debt, the key aggregates for assessing performance against the golden rule and the sustainable investment rule, respectively;
- projections of public sector net borrowing, the fiscal aggregate relevant to assessing the impact of fiscal policy on the economy;
- projections of the cyclically-adjusted fiscal balances; and
- detailed analyses of the outlook for government receipts and expenditure.

C2 The fiscal projections continue to be based on deliberately cautious key assumptions audited by the National Audit Office (NAO).

MEETING THE FISCAL RULES

C3 Table C1 shows five-year projections for the current budget and public sector net debt, the key aggregates for assessing performance against the golden rule and the sustainable investment rule respectively. Outturns and projections for other important measures of the public finances, including net borrowing and cyclically-adjusted fiscal balances, are also shown.

C4 As explained in Chapter 2, the Government's provisional view is that the current economic cycle began in mid-1999. The economy is expected to return to trend around the end of 2005, in line with the forecast in the 2004 Pre-Budget Report.

Table CI: Summary of public sector finances

	Per cent of GDP							
	Outturns		Estimate	Projections				
	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Fairness and prudence								
Surplus on current budget	-1.3	-1.8	-1.4	-0.5	0.0	0.3	0.6	0.8
Average surplus since 1999-2000	1.0	0.5	0.1	0.1	0.1	0.1	0.1	0.2
Cyclically-adjusted surplus on current budget	-0.7	-1.0	-0.8	-0.3	0.1	0.3	0.6	0.8
Long-term sustainability								
Public sector net debt ¹	31.5	32.8	34.4	35.5	36.2	36.8	37.1	37.1
Core debt ¹	31.1	31.6	32.8	33.8	34.5	35.2	35.6	35.7
Net worth ²	23.8	24.7	22.1	19.9	18.9	18.2	18.4	18.0
Primary balance	-0.8	-1.5	-1.3	-0.9	-0.5	-0.2	0.1	0.3
Economic impact								
Net investment	1.1	1.3	1.6	2.1	2.3	2.3	2.3	2.3
Public sector net borrowing (PSNB)	2.4	3.2	2.9	2.6	2.2	2.0	1.6	1.5
Cyclically-adjusted PSNB	1.8	2.3	2.4	2.4	2.2	2.0	1.6	1.5
Financing								
Central government net cash requirement	2.1	3.5	3.7	3.2	2.6	2.3	2.1	2.2
Public sector net cash requirement	2.3	3.5	3.2	2.8	2.4	2.1	1.8	1.8
European commitments								
Treaty deficit ³	2.2	3.2	2.9	2.6	2.2	2.0	1.7	1.6
Cyclically-adjusted Treaty deficit ³	1.6	2.3	2.3	2.4	2.2	2.0	1.7	1.6
Treaty debt ratio ⁴	37.7	39.5	41.0	42.0	42.4	42.8	42.9	42.9
Memo: Output gap	-1.2	-1.2	-0.7	-0.1	0.0	0.0	0.0	0.0

¹ Debt at end March; GDP centred on end March.

² Net worth at end December; GDP centred on end December.

³ General government net borrowing on a Maastricht basis.

⁴ General government gross debt measured on a Maastricht basis.

The golden rule C5 The projections show that the Government is meeting the golden rule, on the basis of cautious assumptions, with an average annual surplus on the current budget over this economic cycle of 0.1 per cent of Gross Domestic Product (GDP). On this basis, and based on cautious assumptions, there is a margin against the golden rule of £6 billion in this cycle, including the Annual Managed Expenditure (AME) margin.

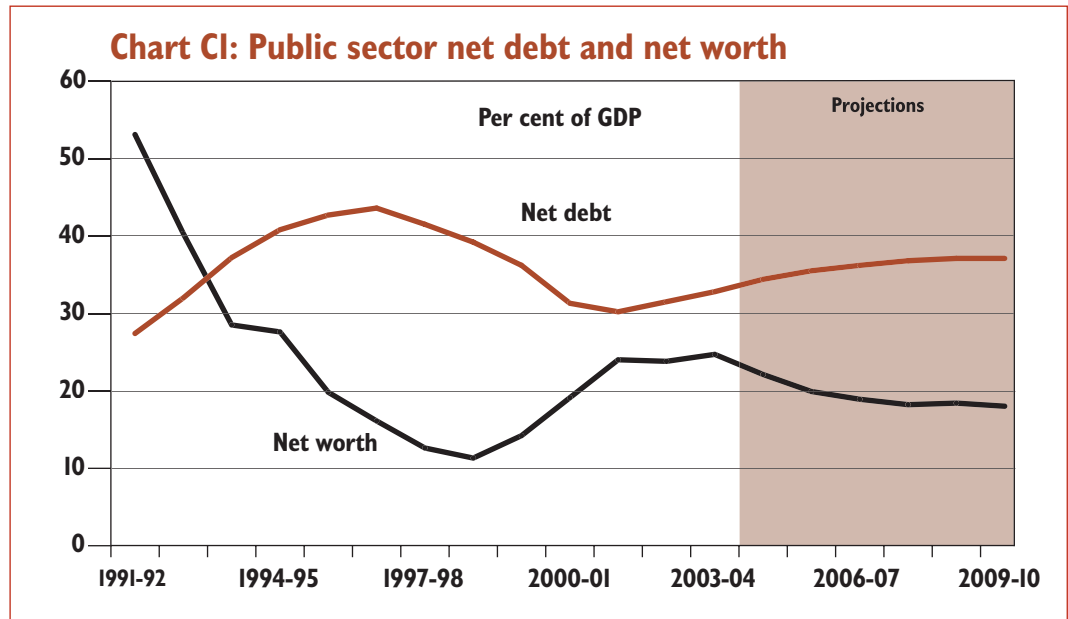
C6 Recent economic developments have been consistent with the current economic cycle drawing to a close around the end of 2005. With the economy assumed to be on trend from then on, the projections show, based on cautious assumptions, that the average surplus on the current budget over the period 2005-06 to 2009-10 is a $\frac{1}{4}$ per cent of GDP. Based on cautious assumptions, the Government is therefore on course to meet the golden rule from 2005-06 to the end of the projection period.

The sustainable investment rule C7 The sustainable investment rule is also met over the economic cycle. In 1996-97, public sector net debt stood at 44 per cent of GDP. The tough decisions on taxation and expenditure taken by the Government, including the decision to use the proceeds from the auction of spectrum licenses to repay debt, reduced debt to around 30 per cent of GDP by the end of 2001-02. It is now projected to rise slowly, as the Government borrows modestly to fund increased investment in public services, reaching 35½ per cent of GDP by the end of this economic cycle, £57 billion below the 40 per cent level, and stabilising at around 37 per cent

of GDP by the end of the projection period. The projections for core debt, which exclude the estimated impact of the economic cycle on public sector net debt, rise to 35½ per cent of GDP by the end of the projection period. This is consistent with the fiscal rules, and with the key objective of intergenerational fairness that underpins the fiscal framework.

Net worth C8 Net worth is the approximate stock counterpart of the current budget. Modest falls in net worth are expected for the remainder of the projection period from the high level of 25 per cent of GDP in 2001-02. At present, net worth is not used as a key indicator of the public finances, mainly as a result of the difficulties involved in accurately measuring many government assets and liabilities.

C9 Chart C1 shows public sector net debt and net worth as a per cent of GDP from 1991-92 to 2009-10



Net investment C10 As a result of decisions taken in the 2004 Spending Review, public sector net investment is projected to rise to 2¼ per cent of GDP by 2007-08. This increase is sustainable and fully consistent with the Government’s long-term approach and the fiscal rules, since net debt is being held at a stable and prudent level over the cycle, well below 40 per cent of GDP.

Net borrowing C11 This increase in net investment, together with the new projections for the current budget, mean that public sector net borrowing is expected to be just under 3 per cent of GDP in 2004-05 and then fall steadily to around 1½ per cent of GDP in 2009-10. Cyclically-adjusted net borrowing in 2004-05 is around 2½ per cent of GDP.

Financing C12 The central government net cash requirement was 3.5 per cent of GDP in 2003-04. It is projected to increase to 3.7 per cent in 2004-05, and decrease to 2.2 per cent of GDP by 2009-10.

European commitments C13 Table C1 shows the Treaty measures of debt and deficit used for the purposes of the Stability and Growth Pact under Article 104 of the Treaty.

CHANGES TO THE FISCAL BALANCES

CI4 Table C2 compares the latest estimates for the main fiscal balances with those in the 2004 Pre-Budget Report and in Budget 2004.

Table C2: Fiscal balances compared with Budget 2004 and the 2004 Pre-Budget Report

	Outturn ¹	Estimate ²	Projections				
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Surplus on current budget (£ billion)							
Budget 2004	-21.3	-10.5	-5	0	4	9	
Effect of revisions and forecasting changes:	0.2	-1.2	-1	1	-1/2	-1	
Effect of discretionary changes	0.0	-0.8	-1/2	0	-1/2	0	
PBR 2004	-21.1	-12.5	-7	1	4	9	12
Effect of revisions and forecasting changes:	0.8	-3.2	1	0	1	-1/2	1/2
Effect of discretionary changes	0.0	0.3	1/2	0	-1/2	1/2	-1/2
Budget 2005	-20.4	-16.1	-6	1	4	9	12
Net borrowing (£ billion)							
Budget 2004	37.5	32.9	31	27	27	23	
Changes to current budget	-0.2	2.0	1/2	-1/2	1/2	1/2	
Forecasting changes to net investment	-2.5	-0.7	1/2	2	1/2	0	
PBR 2004	34.8	34.2	33	29	28	24	22
Changes to current budget	-0.8	3.6	-1	0	-1/2	0	-1/2
Forecasting changes to net investment	1.4	-3.4	-1/2	0	0	0	0
Budget 2005	35.4	34.4	32	29	27	24	22
Cyclically-adjusted surplus on current budget (per cent of GDP)							
Budget 2004	-1.0	-0.2	-0.2	0.0	0.3	0.7	
PBR 2004	-1.0	-0.4	-0.4	0.1	0.3	0.6	0.8
Budget 2005	-1.0	-0.8	-0.3	0.1	0.3	0.6	0.8
Cyclically-adjusted net borrowing (per cent of GDP)							
Budget 2004	2.4	2.1	2.3	2.1	1.9	1.6	
PBR 2004	2.2	2.2	2.5	2.2	2.0	1.6	1.5
Budget 2005	2.3	2.4	2.4	2.2	2.0	1.6	1.5
Net debt (per cent of GDP)							
Budget 2004	33.2	34.4	35.3	35.9	36.3	36.4	
PBR 2004	32.9	34.3	35.4	36.2	36.8	37.0	37.1
Budget 2005	32.8	34.4	35.5	36.2	36.8	37.1	37.1

¹ The 2003-04 figures were estimates in Budget 2004.

² The 2004-05 figures were projections in Budget 2004

Changes between Budget 2004 and the Pre-Budget Report

CI5 In the 2004 Pre-Budget Report, the current budget was revised down in 2004-05 and 2005-06 because of forecasting changes, mainly to receipts, with corporation tax showing the largest changes.

CI6 Discretionary changes, led to further small reductions in the current budget, with a continuation of the freeze of the Budget 2004 increase on road fuel duties, the ten year strategy for childcare and a further addition to the special reserve to meet the costs of the military conflict in Iraq and the UK's other international commitments. These factors offset action taken to combat tax fraud and avoidance.

Changes between the Pre-Budget Report and Budget 2005

CI7 For the public sector current budget the estimated 2004-05 outturn shows a deficit of £16.1 billion around £3½ billion higher than the deficit of £12.5 billion projected in the 2004 Pre-Budget Report. This is largely as a result of higher than expected current expenditure, in part due to a timing effect relating to net payments to the EU, with higher than expected payments in 2004-05 being offset by lower payments in 2005-06. There has been additional expenditure in 2004-05 to meet the UK's international commitments, including a further increase in the special reserve, as well as use by departments of end-year flexibility to meet the Government's priorities including health and education. Use of end-year flexibility has enabled departments to smooth their expenditure for 2004-05, the year with the lowest overall planned spending growth of the

2002 Spending Review period. Underpinned by a strong and stable economy, receipts growth has strengthened through the year, with estimated growth in tax receipts in 2004-05 as projected in the Pre-Budget Report. Growth in corporation tax receipts has exceeded expectations. Non-tax receipts are expected to be around £1 billion lower.

C18 Forecasting changes lead to a small improvement in the 2005-06 current surplus since the 2004 Pre-Budget Report. Receipts are expected to be lower by around £2 billion but current spending in 2005-06 is also expected to be about £2½ billion lower than in the 2004 Pre-Budget Report, partly because of the timing change relating to net payments to the EU and partly because of the resetting of the AME margin. There are also fiscally neutral changes, which reduce both current receipts and spending by around £¾ billion. In subsequent years forecasting changes have little effect on overall current receipts and expenditure.

C19 Discretionary measures announced in this Budget include a commitment to increase the child element of the Child Tax Credit in line with average earnings up to 2007-08, an additional payment guaranteeing that council tax paying households with someone over 65 will receive £200 towards the cost of council tax and further reforms to modernise the tax system. Full details are set out in Chapter A. Overall these changes have only a small effect on the current budget.

C20 Public sector net borrowing in 2004-05 is broadly unchanged compared with the 2004 Pre-Budget Report, due to offsetting impacts of higher current expenditure and lower than expected net investment. This reflects monthly outturns to date.

FORECAST DIFFERENCES AND RISKS

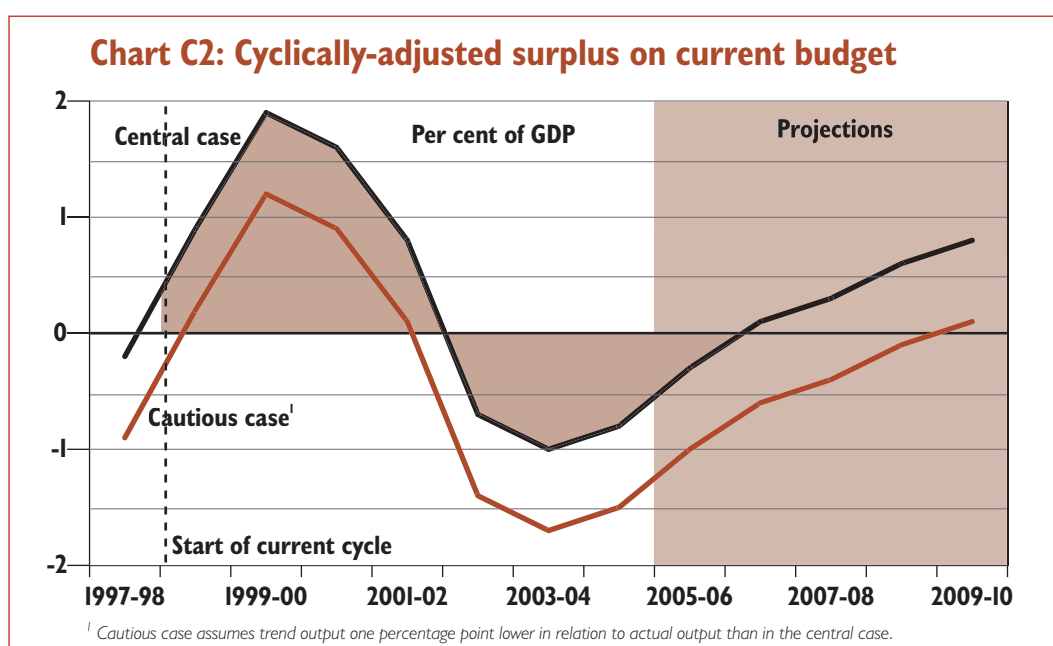
C21 The fiscal balances represent the difference between two large aggregates of expenditure and receipts, and forecasts are inevitably subject to a considerable degree of uncertainty. Over the past ten years, the average absolute difference between year-ahead forecasts of net borrowing and subsequent outturns has been around 1 per cent of GDP. This difference tends to grow as the forecast horizon lengthens. A full account of differences between the year-ahead projections made in Budget 2003 and Budget 2004, and the subsequent outturns is provided in the *End of year fiscal report*, published alongside the 2004 Pre-Budget Report.

C22 As explained in Chapter B, UK GDP expanded by over 3 per cent in 2004, above its assumed trend rate. With world growth maintaining much of its momentum from 2004 and UK business and consumer confidence strong, both external and domestic demand are forecast to grow robustly in the short term. GDP is expected to grow by 3 to 3½ per cent in 2005 as the remaining slack in the economy is absorbed and the output gap is closed around the end of the year. Growth is then expected to be 2½ to 3 per cent in 2006, in line with the economy's trend rate.

C23 The global outlook remains a key influence on UK economic prospects. The risks to the global outlook of higher oil prices have diminished since the Pre-Budget Report given the robustness of growth in the face of higher prices in 2004. The risks relating to exchange rates and the potential for a disorderly adjustment to the world's current account imbalances remain unchanged since the Pre-Budget Report. UK house prices continue to pose risks in both directions, although increasingly the evidence since the Pre-Budget Report points to an orderly moderation in house price inflation and recent signs of some emerging revival in sentiment suggest that the downside risks are smaller than at the time of the Pre-Budget Report. The forecast also continues to face upside risks from investment. For example, growth of business investment could exceed expectations going forward given current robust rates of demand growth and with supportive corporate financial conditions.

C24 The use of cautious assumptions audited by the NAO builds a safety margin into the public finance projections to guard against unexpected events. One of the key audited assumptions is that for trend output growth, which is assumed to be $\frac{1}{4}$ per cent below the neutral view. This means that the rate of economic growth used to forecast the public finances is the bottom end of the projection range. For example, in this Budget, the forecast for economic growth used in the public finances projections over the period 2005-06 averages under $2\frac{1}{2}$ per cent, $\frac{1}{4}$ per cent below the central case. This implies that the level of GDP used in the public finances forecast is 1.3 per cent below the central view by 2009-10.

C25 Another source of potential errors results from misjudging the position of the economy in relation to trend output. To minimise this risk, the robustness of the projections is tested against an alternative scenario in which the level of trend output is assumed to be one percentage point lower than in the central case. Chart C2 illustrates the Budget projection for this cautious case.



C26 The Government has used the cautious case and cautious, audited assumptions to build a safety margin against unexpected events. This was combined with the decision to consolidate the public finances when the economy was above trend, which resulted in low debt. This has allowed the Government to safeguard the increase in investment in priority public services, allow the automatic stabilisers to work in full during the period of global economic uncertainty in the early part of the decade and meet in full the UK's international commitments, while continuing to meet the fiscal rules.

ASSUMPTIONS

C27 The fiscal projections are based on the following assumptions:

- the economy follows the path described in Chapter B. In the interests of caution, the fiscal projections continue to be based on the deliberately prudent and cautious assumption of trend output growth of $2\frac{1}{2}$ per cent up to 2006-07, $\frac{1}{4}$ percentage point lower than the Government's neutral view. The Government's neutral view of trend output is reduced to $2\frac{1}{2}$ per cent between 2007-08 and 2009-10, and so, to maintain a cautious approach, an assumption of $2\frac{1}{4}$ per cent is used in the public finances projections, still $\frac{1}{4}$ percentage point lower than the Government's neutral view;

- there are no tax or spending policy changes beyond those announced in or before this Budget, and the indexation of rates and allowances;
- firm Departmental Expenditure Limits (DEL) as set out in the 2004 Spending Review up to 2007-08, but adjusted for the impact of policy decisions and reclassifications;
- total AME programmes through to 2005-06 have been reviewed. The total has been adjusted for DEL/AME reclassifications, and for the estimated costs of spending measures announced in this Budget. In accordance with usual practice, the Government has decided to reset the AME margin to zero in 2004-05, £1 billion in 2005-06, £2 billion in 2006-07 and £3 billion in 2007-08;
- as is normal, the Treasury is setting out its assumption for public sector current expenditure for the period beyond the next Spending Review. Public sector current expenditure in 2008-09 is assumed to grow by 1.9 per cent in real terms, in line with the assumed growth rate in the 2004 Pre-Budget Report, and by the same rate in 2009-10. Taken together, these assumptions imply public sector current expenditure grows on average in line with the cautious view of trend GDP growth used in the public finance projections for the three year period starting in 2007-08; and
- Net investment is assumed to remain at 2¼ per cent of GDP in 2008-09 and 2009-10.

Table C3: Economic assumptions for the public finance projections

	Percentage changes on previous year						
	Outturn	Estimate	Projections				
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Output (GDP)	2½	3¼	3	2½	2¼	2¼	2¼
Prices							
CPI	1¼	1½	1¼	2	2	2	2
GDP deflator	3	2	2½	2¾	2¾	2¾	2¾
RPI ¹ (September)	3	3	2¾	2½	2¾	2¾	2¾
Rossi ² (September)	2	1¼	2	2½	2¼	2¼	2¼
Money GDP ³ (£ billion)	1,118	1,174	1,240	1,305	1,369	1,437	1,507

¹ Used for revalorising excise duties in current year and uprating income tax allowances and bands and certain social security benefits in the following year.

² RPI excluding housing costs, used for uprating certain social security benefits.

³ Not seasonally adjusted.

C28 Consistent with the *Code for fiscal stability*, the forecast does not take account of measures proposed in this Budget for consultation or other proposals where final decisions have yet to be taken such as the rollout of the local housing allowance to the private and social rented sectors, further extensions to paid maternity leave or increasing Child Trust Fund Payments, or others where the impact cannot yet be quantified, such as the Pension Protection Fund. The Government is also awaiting the judgement from the Law Lords on a recent case regarding state pensions for pensioners living outside the EU;

C29 The outturn figures are based on series published in the monthly Public Sector Finance release (the latest outturns covering January 2005 were published on 18th February 2005). The figures are also adjusted to take account of the changes announced by the Office for National Statistics (ONS), where the size of the change has also been publicly announced. This includes the revisions concerning roads maintenance expenditure detailed in ONS's Technical Explanatory Note published on 28 February 2005.

C30 The projections for 2004-05 also are based on all data available within the Treasury and other departments involved in producing tax and spending forecasts where the projections were finalised. This includes details of February central government receipts and spending which will form the basis of the February outturn numbers to be published by ONS and HM Treasury on 18 March 2005.

C31 The key assumptions underlying the fiscal projections are audited by the National Audit Office (NAO) under the three-year rolling review process. Details of the audited assumptions are given in Box C1.

Box C1: Key assumptions audited by the NAO^a

<ul style="list-style-type: none"> • Privatisation proceeds • Trend GDP growth • UK claimant recent unemployment^d • Interest rates • Equity prices^b • VAT^{b,c} • Consistency of price indices^b • Composition of GDP^c • Funding^c • Oil prices • Tobacco 	<p>Credit is taken only for proceeds from sales that have been announced.</p> <p>2½ per cent a year to 2006-07 and 2¼ per cent in subsequent years.</p> <p>Rising slowly to 0.89 million in 2007-08, from recent levels of 0.82 million.</p> <p>3-month market rates change in line with market expectations (as of 7 March).</p> <p>FTSE All-share index rises from 2523 (close 7 March) in line with money GDP.</p> <p>The VAT gap will rise by 0.5 percentage points per year from a level that is at least as high as the estimated outturn for the current year.</p> <p>Projections of price indices used to project the public finances are consistent with CPI.</p> <p>Shares of labour income and profits in national income are broadly constant in the medium term.</p> <p>Funding assumptions used to project debt interest are consistent with the forecast level of government borrowing and with financing policy.</p> <p>\$40.6 a barrel in 2005, the average of independent forecasts, and then constant in real terms.</p> <p>The underlying market share of smuggled cigarettes will be set at least at the latest published outturn. For Budget 2005, a share of 14.5 per cent is used for 2005-06 onwards.</p>
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^a For details of all NAO audits before the 2003 Pre-Budget Report, see Budget 2003, 9 April 2003 (HC500).

^b Audit of Assumptions for the 2003 Pre-Budget Report, 10 December 2003 (HC35).

^c Audit of Assumptions for the 2004 Budget, 17 March 2004 (HC434)

^d Audit of Assumptions for the 2005 Budget, 16 March 2005 (HC452)

The audited assumptions

C32 For this Budget, the Comptroller and Auditor General audited the assumption on UK claimant unemployment, under the three year rolling review process. The review concluded that the assumption was reasonable and cautious. The public finances continue to be based

on a deliberately cautious assumption for trend output growth that is a $\frac{1}{4}$ percentage point lower than the Government's neutral view. The Comptroller and Auditor General will be invited to audit this assumption once the current cycle has ended, currently projected to be around the end of 2005, around which time information relating to an additional on-trend point will be available.

FISCAL AGGREGATES

C33 Tables C4 and C5 provide more detail on the projections for the current and capital budgets.

Table C4: Current and capital budgets

	£billion						
	Outturn	Estimate	Projections				
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Current budget							
Current receipts	418.9	449.7	487	520	553	582	612
Current expenditure	425.3	451.1	477	503	531	555	581
Depreciation	14.0	14.6	15	16	17	18	19
Surplus on current budget	-20.4	-16.1	-6	1	4	9	12
Capital budget							
Gross investment	35.7	38.8	47	51	53	56	58
Less asset sales	-6.7	-5.8	-5	-5	-5	-5	-4
Less depreciation	-14.0	-14.6	-15	-16	-17	-18	-19
Net investment	15.0	18.3	26	29	31	32	34
Net borrowing	35.4	34.4	32	29	27	24	22
Public sector net debt- end year	375.5	415.0	452	484	517	546	573
Memos:							
Treaty deficit ¹	35.4	34.1	32	29	27	24	24
Treaty debt ²	441.2	481.5	521	554	587	617	647

¹General government net borrowing on a Maastricht basis.

²General government gross debt on a Maastricht basis.

Table C5: Current and capital budgets

	Per cent of GDP						
	Outturn	Estimate	Projections				
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Current budget							
Current receipts	37.5	38.3	39.3	39.9	40.4	40.5	40.6
Current expenditure	38.1	38.4	38.5	38.6	38.8	38.6	38.5
Depreciation	1.3	1.2	1.2	1.3	1.3	1.3	1.3
Surplus on current budget	-1.8	-1.4	-0.5	0.0	0.3	0.6	0.8
Capital budget							
Gross investment	3.2	3.3	3.8	3.9	3.9	3.9	3.9
Less asset sales	-0.6	-0.5	-0.4	-0.4	-0.4	-0.3	-0.3
Less depreciation	-1.3	-1.2	-1.2	-1.3	-1.3	-1.3	-1.3
Net investment	1.3	1.6	2.1	2.3	2.3	2.3	2.3
Net borrowing	3.2	2.9	2.6	2.2	2.0	1.6	1.5
Public sector net debt- end year	32.8	34.4	35.5	36.2	36.8	37.1	37.1
Memos:							
Treaty deficit ¹	3.2	2.9	2.6	2.2	2.0	1.7	1.6
Treaty debt ratio ²	39.5	41.0	42.0	42.4	42.8	42.9	42.9

¹General government net borrowing on a Maastricht basis.

²General government gross debt on a Maastricht basis.

C34 Following a current budget deficit of 3 per cent of GDP in 1996-97, current budget surpluses of more than 2 per cent were recorded in 1999-2000 and 2000-01. These surpluses allowed the Government to use fiscal policy to support monetary policy during the economic slowdown in 2001 and 2002, and as a result the current budget moved into deficit. The current budget is expected to move back into surplus in 2006-07, with increasingly larger surpluses in later years, reaching 0.8 per cent in 2009-10.

C35 The current budget surplus is equal to public sector current receipts minus public sector current expenditure and depreciation. Underlying the projections of the current budget are steady increases in the ratio of current receipts to GDP. This partly reflects measures taken to protect revenues. The other reasons behind this are explained in later sections.

C36 Table C4 also shows that net investment is projected to increase from £15 billion in 2003-04 to £31 billion in 2007-08, as the Government seeks to rectify historical under-investment in public infrastructure. These increases are sustainable and fully consistent with the Government's long-term approach and the fiscal rules, as debt is being held at 37 per cent of GDP or less throughout the projection period, well within the 40 per cent limit set by the sustainable investment rule.

RECEIPTS

C37 This section looks in detail at the projections for public sector tax receipts. It begins by looking at the main determinants of changes in the overall projections since the 2004 Pre-Budget Report, before looking in detail at changes in the projections of individual tax receipts. Finally, it provides updated projections for the tax-GDP ratios.

Changes in total receipts since the 2004 Pre-Budget Report

C38 Table C6 provides a detailed breakdown of the main factors that have led to the changes in the overall projections since the 2004 Pre-Budget Report.

Table C6: Changes in current receipts since the 2004 Pre-Budget Report

	£ billion					
	Estimate		Projections			
	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Effect on receipts of non-discretionary changes in:						
Assumptions audited by the NAO	0	1	2	2	2	2
Other economic determinants	-1	-1	-1	0	½	½
Fiscal forecasting changes	-½	-2	-2	-2	-3	-2
Total before discretionary changes¹	-1½	-2	-1	0	-1	0
Discretionary changes ²	0	1½	1	1½	1	½
Total change¹	-1½	-½	½	1	0	½

¹ Totals may not sum due to rounding.

² Includes measures announced since the 2004 Pre-Budget Report.

Economic determinants audited by the NAO **C39** Changes in economic determinants audited by the NAO increase public sector current receipts by around £1 billion in 2005-06 and by a little under £2 billion over the rest of the forecast period. Higher profiles for dollar oil prices, equity prices and interest rates all contribute to higher receipts. The average of independent forecasts for 2005 has risen from \$38.2 a barrel used in the 2004 Pre-Budget Report to \$40.6 a barrel. The impact on North Sea revenues is limited due to the appreciation of sterling against the dollar, which means the increase in sterling terms is more modest. The impact of the exchange rate is included in other economic determinants.

C40 Compared to the 2004 Pre-Budget Report, equity prices are around 4 per cent higher throughout the forecast period. This adds around £½–£1 billion to receipts from corporation tax revenues from life assurance companies, stamp duty receipts and capital taxes. Income tax on interest income is higher because of the NAO assumption on interest rates.

Other economic determinants C41 Changes in other economic determinants subtract around £1 billion in 2004-05. This in part reflects lower than expected estimates of wages and salaries in 2004 based on provisional data, although PAYE and National Insurance contributions for 2004-05 are estimated to be in line with their 2004 Pre-Budget Report estimate. It also reflects slower growth in the GDP components that are used to project the VAT tax base, including modestly lower growth in nominal consumers' expenditure. In later years, the impact of these factors diminishes and there is a boost from higher estimates of North Sea oil production.

Fiscal forecasting changes C42 Fiscal forecasting changes account for around £½ billion of the reduction in receipts in 2004-05 and around £1-2 billion in subsequent years. The 2004-05 reduction represents the combined effects of many different changes, largely reflecting outturns for the year to date. In subsequent years, the change is larger partly reflecting the effect of fiscally neutral changes, which reduce both receipts and spending by about £½ billion in 2005-06 and 2006-07 and by about £1 billion a year in subsequent years. They also reflect lower non-tax receipts, particularly from public corporations.

Tax-by-tax analysis

C43 Table C7 shows the changes to the projections of individual taxes since Budget 2004 and the 2004 Pre-Budget Report for 2004-05 and 2005-06. The table shows that overall net taxes and national insurance contributions are as forecast in the Pre-Budget Report. Table C8 contains updated projections for the main components of public sector receipts for 2003-04, 2004-05 and 2005-06.

Table C7: Changes in current receipts by tax since Budget 2004 and the 2004 Pre-Budget Report

	£ billion			
	Budget 2004		PBR 2004	
	2004-05	2005-06	2004-05	2005-06
Income tax (gross of tax credits)	-1.0	0.7	-0.6	0.3
National Insurance Contributions	0.2	0.4	0.1	0.3
Non-North Sea corporation tax ¹	-2.1	-1.2	1.0	1.2
Less tax credits ²	-0.5	-0.3	-0.4	-0.2
North Sea revenues	1.6	3.4	-0.1	1.1
Capital taxes ³	0.9	1.2	0.3	0.3
Stamp duty	-0.5	-0.8	0.1	0.1
Value added tax	-0.8	-1.1	-1.2	-1.0
Excise duties ⁴	-0.7	-1.0	-0.1	-0.2
Other taxes and royalties ⁵	-1.0	-3.0	0.7	-1.3
Net taxes and National Insurance contributions	-3.8	-1.7	0.1	0.7
Other receipts and accounting adjustments	-1.2	-1.4	-1.4	-1.1
Current receipts	-5.0	-3.1	-1.3	-0.3

¹ National accounts measure: gross of enhanced and payable tax credits.

² Includes enhanced company tax credits that offset tax liability.

³ Capital gains tax and inheritance tax.

⁴ Fuel, alcohol and tobacco duties.

⁵ Includes council tax and money paid into the National Lottery Distribution Fund, as well as other central government taxes.

Table C8: Current receipts

	£ billion		
	Outturn 2003-04	Estimate 2004-05	Projection 2005-06
<i>Inland Revenue</i>			
Income tax (gross of tax credits)	118.4	126.8	138.1
Income tax credits	-4.5	-4.1	-3.9
National Insurance Contributions	72.5	77.9	82.6
Corporation tax ¹	28.6	34.1	43.7
Corporation tax credits ²	-0.5	-0.5	-0.5
Petroleum revenue tax	1.2	1.3	1.5
Capital gains tax	2.2	2.3	3.0
Inheritance tax	2.5	2.9	3.4
Stamp duties	7.5	8.9	9.7
Total Inland Revenue (net of tax credits)	228.0	249.6	277.5
<i>Customs and Excise</i>			
Value added tax	69.1	72.3	76.3
Fuel duties	22.8	23.5	24.6
Tobacco duties	8.1	8.1	8.4
Spirits duties	2.4	2.4	2.5
Wine duties	2.0	2.2	2.3
Beer and cider duties	3.2	3.3	3.4
Betting and gaming duties	1.3	1.4	1.4
Air passenger duty	0.8	0.9	1.0
Insurance premium tax	2.3	2.4	2.6
Landfill tax	0.6	0.7	0.7
Climate change levy	0.8	0.8	0.8
Aggregates levy	0.3	0.3	0.3
Customs duties and levies	1.9	2.2	2.2
Total Customs and Excise	115.7	120.4	126.5
Vehicle excise duties	4.8	4.8	5.1
Oil royalties	0.0	0.0	0.0
Business rates ³	18.3	19.0	19.4
Council tax ⁴	18.8	19.8	20.9
Other taxes and royalties ⁵	11.2	12.0	12.4
Net taxes and National Insurance contributions⁶	396.8	425.6	461.9
Accruals adjustments on taxes	3.2	2.3	0.9
Less own resources contribution to European Communities (EC) budget	-4.6	-4.0	-3.9
Less PC corporation tax payments	-0.1	-0.1	-0.1
Tax credits adjustment ⁷	0.5	0.6	0.6
Interest and dividends	4.4	5.0	4.9
Other receipts ⁸	18.5	20.2	22.4
Current receipts	418.9	449.7	486.7
<i>Memo:</i>			
North Sea revenues ⁹	4.3	5.2	7.1

¹ National accounts measure: gross of enhanced and payable tax credits.

² Includes enhanced company tax credits.

³ Includes district council rates in Northern Ireland paid by business.

⁴ Cash numbers. The increase in accrued council tax in 2005-06 is based on the latest available estimates released by the Chartered Institute for Public Finance and Accountancy (CIPFA) and the increases for later years on the increases in council tax from 1993-94 onwards.

⁵ Includes VAT refunds and money paid into the National Lottery Distribution Fund.

⁶ Includes VAT and 'traditional own resources' contributions to EC budget.

⁷ Tax credits which are scored as negative tax in the calculation of NTNIC but expenditure in the national accounts.

⁸ Includes gross operating surplus and rent; net of oil royalties and business rate payments by Local Authorities.

⁹ Consists of North Sea corporation tax, petroleum revenue tax and royalties.

Income tax and national insurance contributions **C44** Accrued income tax and NICs for 2004-05 is only slightly below the 2004 Pre-Budget Report projection. The 2004 Pre-Budget Report forecast for 2004-05 was based on growth in cash receipts of income tax, national insurance contributions and capital gains tax increasing from 7.1 per cent for April-October 2004 to 7.8 per cent for 2004-05 as a whole. Cash receipts to the end of January were running ahead of this showing growth of 8.8 per cent on the same period in 2003-04. However, this largely reflected a timing shift, as a larger proportion of self-assessment receipts due on 31 January are expected to score in January in 2005 than in 2004, because the due date was a Monday in 2005 and a Saturday in 2004. Self assessment receipts for the year as a whole are expected to be around £½ billion lower than in the 2004 Pre-Budget Report. There is a larger shortfall on the income tax and national insurance contributions (NIC) elements of self-assessment, because the capital gains tax element is expected to be slightly higher.

C45 In contrast, receipts from Pay As You Earn (PAYE) income tax and Class 1 NICs are in line with their 2004 Pre-Budget Report estimate, which was based on a further recovery in bonus payments, particularly in the financial sector. Budget 2005 reiterates the Government's intention, announced alongside the 2004 Pre-Budget Report, to close down permanently the ever more complex and contrived attempts at tax and NICs avoidance, particularly in relation to financial sector bonuses. Other income tax components, such as tax on interest income have grown more quickly than expected since the 2004 Pre-Budget Report. Receipts from income tax and NICs are expected to be a little stronger in 2005-06. This chiefly reflects the economic determinants including higher revenues from the interest rate assumption audited by the NAO.

Non-North Sea corporation tax **C46** In the 2004 Pre-Budget Report, year on year growth of total corporation tax receipts was expected to increase from 12.5 per cent for the April to October period to 15.3 per cent for the year as a whole. Since the 2004 Pre-Budget Report, receipts have grown more quickly than expected, with year on year growth from April to January of 17.4 per cent. With North Sea corporation tax in line with expectations in January, the higher than anticipated growth is due to non-North Sea companies. Total receipts for non North Sea corporation tax in 2004-05 are now estimated to be just over £1 billion higher than in the Pre-Budget Report. Receipts were stronger than expected from both industrial and financial companies.

C47 Further above trend growth is expected in 2005, as the remaining slack in the economy is absorbed. This should continue to boost receipts through 2005-06. Receipts growth in 2005-06 should also benefit from financial company taxable profits returning towards trend, the impact of higher equity prices on receipts from life assurance companies and the impact from of anti-avoidance measures announced in the 2005 Budget and in earlier Budgets and Pre-Budget Reports.

North Sea revenues **C48** The 2004 Pre-Budget Report noted that the full impact of higher oil prices on North Sea revenues would not be reflected in receipts until towards the end of 2004-05, because of lags built into the tax system. For North Sea corporation tax, the full effect would not be seen until the instalment payments in January and April 2005. North Sea corporation tax receipts were, as expected, much higher in January 2005 than in January 2004 and overall North Sea receipts in 2004-05 are expected to be close to their Pre-Budget Report estimate.

C49 The forecast for North Sea revenues uses the NAO audited assumption on oil prices. Oil prices are expected to average \$40.6 a barrel in 2005, in line with the average of independent forecasts. This is substantially below the oil price level in the first quarter of 2005. Compared with the 2004 Pre-Budget Report, oil prices are expected to be \$2.4 a barrel higher in 2005, although the appreciation in sterling against the dollar means that the rise in sterling terms is less marked. The Budget 2005 changes to the payment profile of North Sea corporation tax bring the average lag before tax is due more into line with the PRT lag and add around £1.1 billion to overall revenues in 2005-06, whilst the stronger oil price projection, coupled with upward revisions estimates of oil production result in higher North Sea revenue projections from 2005-06 onwards. The scoring of the payment changes is consistent with Eurostat guidance on permanent changes in due for payment dates¹.

Capital gains tax and inheritance tax C50 Initial analysis of the self-assessment returns suggests capital gains tax in 2004-05 is likely to be around £300 million higher than expected in the 2004 Pre-Budget Report. The maturing of the business asset taper in 2002-03 led to larger than expected disposals of business assets, which boosted receipts in 2003-04. The continuation of this trend is likely to be one factor behind the higher than anticipated receipts for 2004-05. Higher equity prices will push up receipts of capital gains tax and inheritance tax combined by around £½ billion, although tax payment lags mean that most of this effect will only be observed from 2006-07 onwards.

Stamp duties C51 The 2004 Pre-Budget Report forecast for stamp duties assumed weaker growth in receipts in the final part of 2004-05 than earlier in the financial year, reflecting the moderation in house price inflation and less buoyant housing market activity. Total receipts for 2004-05 are close to their 2004 Pre-Budget Report estimate. The projection for stamp duty receipts in 2005-06 reflects a more subdued housing market and the impact from the measures to raise the stamp duty threshold to £120,000 and the reform of disadvantaged area relief. A higher equity price projection leads to higher receipts from stamp duty on shares.

VAT receipts C52 VAT receipts on a cash basis in 2004-05 are estimated to be around £1.2 billion below the 2004 Pre-Budget Report projection. Part of the explanation is likely to be slower growth in the GDP components that are used to project the VAT tax base, particularly lower growth in nominal consumers' expenditure. The slower growth in VAT receipts in recent months is consistent with the easing in the growth of nominal retail sales, after a period of greater buoyancy earlier in the year.

Excise duties C53 Higher pump prices, the result of the continued high oil price, has reduced the demand for fuel and lowers revenues from fuel duties, which are charged on a per litre basis. With the oil price expected to remain higher than in the 2004 Pre-Budget Report forecast, fuel duties are likely to be affected further in 2005-06. The decision to delay the revalorisation of fuel duties until September 2005 will also reduce revenues in 2005-06. The 2004 Pre-Budget Report forecast had assumed, in line with convention, that fuel duty rates would rise in line with inflation on the day of the Budget. In contrast, revenues from tobacco duties in 2004-05 are close to the 2004 Pre-Budget Report estimate, whilst alcohol duties have been stronger than expected. This is primarily due to stronger sales of wine.

Council tax C54 Council tax increases are determined annually by local authorities, not by the Government, and the council tax figures for 2005-06 onward are projections based on stylised assumptions, not government forecasts. The methodology used to derive these assumptions is the same as in Budget 2004. The projected increase in 2005-06 is based on the latest available estimates released by the Chartered Institute for Public Finance and Accountancy

¹ ESA95 Manual of Government deficit and debt, Section I 1.2 (Eurostat 2002).

(CIPFA)² and the increases for later years on the average increases in council tax from 1993-94 onwards. These increases are lower than those assumed in the 2004 Pre-Budget Report, with council tax around £½ billion lower in 2005-06 and around £¼ billion lower by 2009-10. However, changes to council tax are broadly balanced by changes to locally financed expenditure and have no material effect on the current balance or net borrowing.

Other taxes and royalties C55 The main change in the 'other taxes' component in 2004-05 is higher than anticipated VAT refunds, which also affect spending estimates. In 2005-06, projections for business rates and vehicle excise duty are lower, whilst VAT refunds are expected to move back in line with the Pre-Budget Report forecast.

Other receipts C56 Non-tax receipts are now expected to be about £1½ billion lower in 2004-05, and about £1 billion a year lower in subsequent years largely because of a reduction in gross operating surpluses. Under national accounts rules, current receipts include gross operating surpluses for all sectors. For non-market bodies, such as most of central government, this is imputed and equals depreciation. For market bodies, such as public corporations, gross operating surplus is derived by adding back depreciation to the net operating surplus. Almost £1/2 billion of the change each year reflects the changes to the treatment of roads maintenance expenditure (see the Assumptions section above), but this change also reduces current spending (accounting adjustments in AME, see the DEL and AME section below) and depreciation itself. It therefore has no effect on net borrowing but has an upward overall impact on the current budget balance. Most of the remainder of the change since the Pre-Budget Report reflects a reduction in public corporation gross (and net) operating surplus, which does impact on the current budget. Very little in-year data is available in the public corporations sector, which includes some 350 different corporations. The data is subject to considerable revision, and will not be finalised until final accounts are available after the end of the financial year.

Tax-GDP ratio

C57 Table C9 shows projections of receipts from major taxes as a per cent of GDP, and Table C10 sets out current and previous projections of the overall tax-GDP ratio.

C58 The tax-GDP ratio is expected to have risen to 36.3 per cent in 2004-05 from 35.6 per cent in 2003-04. This is primarily due to the strong receipts growth in both income tax and non-North Sea corporation tax. Table C7 shows that net taxes and national insurance contributions is little changed from the 2004 Pre-Budget Report, at £425.6 billion. The 0.1 percentage point rise in the tax-GDP ratio mainly reflects lower nominal GDP. The reductions in money GDP also affect later years and explain part of the increases in the tax-GDP ratio since the 2004 Pre-Budget Report. Discretionary changes, mainly those designed to combat tax avoidance and fraud, also impact on the ratio.

C59 The increase in the ratio from 2005-06 onwards is largely driven by rises in the income tax and corporation tax to GDP ratios. The income tax to GDP ratio is driven by the normal fiscal forecasting convention for the treatment of fiscal drag. The rise in the non-North Sea corporation tax to GDP ratio reflects the recovery in receipts from financial company profits, the impact of higher equity prices on receipts from life assurance companies and the anti-avoidance measures announced in this Budget and in previous Budgets and Pre-Budget Reports.

²Published on-line by the Chartered Institute of Public Finance and Accountancy (CIPFA), February 2005, at <http://www.cipfa.org.uk>.

Table C9: Current receipts as a proportion of GDP

	Per cent of GDP						
	Outturn	Estimate	Projections				
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Income tax (gross of tax credits)	10.6	10.8	11.1	11.3	11.5	11.7	11.9
National insurance contributions	6.5	6.6	6.7	6.7	6.8	6.8	6.8
Non-North Sea corporation tax ¹	2.3	2.6	3.1	3.4	3.5	3.5	3.5
Tax credits ²	-0.4	-0.4	-0.4	-0.3	-0.3	-0.3	-0.3
North Sea revenues ³	0.4	0.4	0.6	0.5	0.6	0.5	0.4
Value added tax	6.2	6.2	6.2	6.1	6.1	6.1	6.1
Excise duties ⁴	3.4	3.4	3.3	3.3	3.2	3.2	3.1
Other taxes and royalties ⁵	6.7	6.7	6.7	6.8	6.9	7.0	7.0
Net taxes and national insurance contributions⁶	35.6	36.3	37.3	37.9	38.3	38.5	38.5
Accruals adjustments on taxes	0.3	0.3	0.1	0.1	0.2	0.1	0.1
Less EC transfers	-0.4	-0.3	-0.3	-0.3	-0.3	-0.3	-0.2
Tax credits ⁷	0.0	0.0	0.0	0.0	0.0	0.0	0.1
Other receipts ⁸	1.9	2.1	2.1	2.1	2.1	2.2	2.2
Current receipts	37.5	38.3	39.3	39.9	40.4	40.5	40.6

¹ Gross of enhanced and payable tax credits.

² Tax credits scored as negative tax in net taxes and national insurance contributions.

³ Includes oil royalties, petroleum revenue tax and North Sea corporation tax.

⁴ Fuel, alcohol and tobacco duties.

⁵ Includes council tax and money paid into the National Lottery Distribution Fund, as well as other central government taxes.

⁶ Includes VAT and 'own resources' contributions to EU budget. Cash basis.

⁷ Tax credits scored as negative tax in net taxes and national insurance contributions but expenditure in the national accounts.

⁸ Mainly gross operating surplus and rent, excluding oil royalties. Net of Local Authority business rate payments.

Table C10: Net taxes and national insurance contributions¹

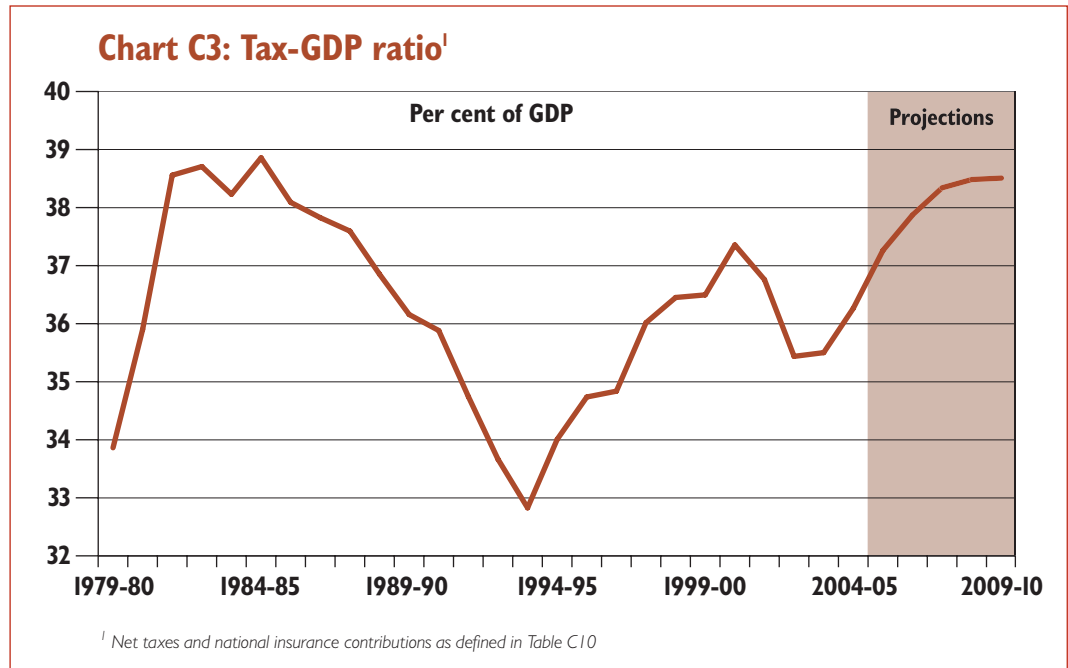
	Per cent of GDP						
	Outturn ²	Estimate ³	Projections				
	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
Budget 2004	35.7	36.5	37.3	37.8	38.1	38.3	
PBR 2004	35.6	36.2	37.1	37.7	38.1	38.3	38.4
Budget 2005	35.6	36.3	37.3	37.9	38.3	38.5	38.5

¹ Cash basis. Uses OECD definition of negative tax credits.

² The 2003-04 figures were estimates in Budget 2004.

³ The 2004-05 figures were projections in Budget 2004.

C60 Chart C3 shows the tax-GDP ratio from 1978-79 to 2009-10.



PUBLIC EXPENDITURE

C60 This section looks in detail at the projections for public expenditure. The spending projections cover the whole of the public sector, using the national accounts aggregate Total Managed Expenditure (TME).

C61 For fiscal aggregates purposes, TME is split into national accounts components covering public sector current expenditure, public sector net investment and depreciation. For budgeting and other purposes, TME is split into Departmental Expenditure Limits (DEL) – firm three year limits for department’s programme expenditure – and Annually Managed Expenditure (AME) – expenditure which is not easily subject to firm multi-year limits.

Changes in TME since 2004 Pre-Budget Report

C62 Forecasting changes have led to lower TME in each year. These changes are described in detail below. Discretionary changes to TME include scorecard measures on pensioners as described in Chapter A and increase spending by about £1 to £1½ billion a year from 2005-06 to 2007-08. Overall, TME is slightly lower in 2004-05 and 2005-06 but unchanged in later years.

C63 Although, as expected in the 2004 Pre-Budget Report, expenditure growth has slowed in the last few months of 2004-05, total current expenditure in 2004-05 is now expected to be about £2½ billion higher, partly due to a timing effect relating to net payments to the EU, with higher than expected payments in 2004-05 being offset by lower expected payments in 2005-06. There has been additional expenditure in 2004-05 to meet the UK's international commitments including special reserve as well as use by departments of end-year flexibility to meet the Government's priorities including health and education. Use of end-year flexibility has enabled departments to smooth their expenditure for 2004-05, the year with the lowest overall planned spending growth of the 2002 Spending Review period. Outturns to date suggest that capital expenditure will be lower than expected in 2004-05, and this change more than offsets the effect of higher current spending, leading to a fall in TME of about £1 billion.

C64 Current spending in 2005-06 is expected to be about £2½ billion lower than in the 2004 Pre-Budget Report. About £2 billion of the change is due to resetting of the AME margin. In the 2004 Pre-Budget Report lower forecasts of AME components and the normal practice of absorbing these changes within set AME total meant that the AME margin rose to almost £3 billion. This has now been reset to £1 billion. The forecasts for AME components has fallen since the 2004 Pre-Budget Report, changes to the timing of net contributions to the EU and lower net spending on public sector pensions national accounts spending offsetting modest increases in other components. Current spending including discretionary changes is little changed from the 2004 Pre-Budget Report after 2005-06.

C65 Public sector current expenditure is increased in 2004-05, but reduced in subsequent years. ONS revisions to the treatment of road maintenance and repair expenditure eliminate the double-count reducing the forecast by £0.4bn in each year. This change also reduces the depreciation forecast and increases public sector net investment by £0.4bn in each year. Other changes are described in detail below.

Table C I I: Total Managed Expenditure 2003–04 to 2007–08

	£ billion				
	Outturn 2003-04	Estimate 2004-05	Projections		
			2005-06	2006-07	2007-08
Departmental Expenditure Limits					
Resource Budget	251.9	268.7	286.9	304.8	320.6
Capital Budget	23.2	23.8	28.8	32.0	35.2
Less depreciation	-9.4	-11.3	-11.8	-12.1	-11.8
Total Departmental Expenditure Limits	266.0	281.2	303.9	324.7	344.0
Annually Managed Expenditure					
Social security benefits ¹	112.7	121.4	127.3	131.6	138.6
Tax credits ¹	14.8	15.2	14.6	14.0	13.9
Common Agricultural Policy	2.9	3.2	3.3	3.2	3.2
Net public service pensions ²	2.0	1.0	0.7	0.3	0.3
National Lottery	1.9	1.8	1.7	1.5	1.3
Non-cash items in AME	5.2	3.4	2.2	3.9	4.5
Other departmental expenditure	1.5	4.2	5.2	3.6	3.4
Net payments to EU institutions ³	2.4	3.7	3.1	2.8	4.5
Locally-financed expenditure	21.2	24.3	25.4	27.1	28.8
Central government gross debt interest	22.2	23.8	25.6	27.0	28.8
Public corporations' own-financed capital expenditure	2.5	2.2	2.3	2.3	2.5
AME margin	0.0	0.0	1.0	2.0	3.0
Accounting adjustments ⁴	-0.9	-1.2	2.3	5.1	3.6
Annually Managed Expenditure	188.4	202.9	214.7	224.5	236.0
Total Managed Expenditure	454.3	484.1	518.6	549.2	580.0
of which:					
Public sector current expenditure	425.3	451.1	476.9	503.4	531.5
Public sector net investment	15.0	18.3	26.2	29.4	31.1
Public sector depreciation	14.0	14.6	15.5	16.4	17.4

¹ For 2003-04 to 2006-07, child allowances in Income Support and Jobseekers' Allowance, which, from 2003-04, are paid as part of the Child Tax Credit, have been included in the tax credits line and excluded from the social security benefits line. This is in order to give figures a consistent definition over the forecast period.

² Net public service pensions expenditure is reported on a national accounts basis.

³ Net payments to EU Institutions exclude the UK's contribution to the cost of EU aid to non-Member States (which is attributed to the aid programme).

Net payments therefore differ from the UK's net contribution to the EU Budget, latest estimates for which are (in £ billion):

	2004-05	2005-06	2006-07	2007-08
	4.3	3.8	3.4	5.2

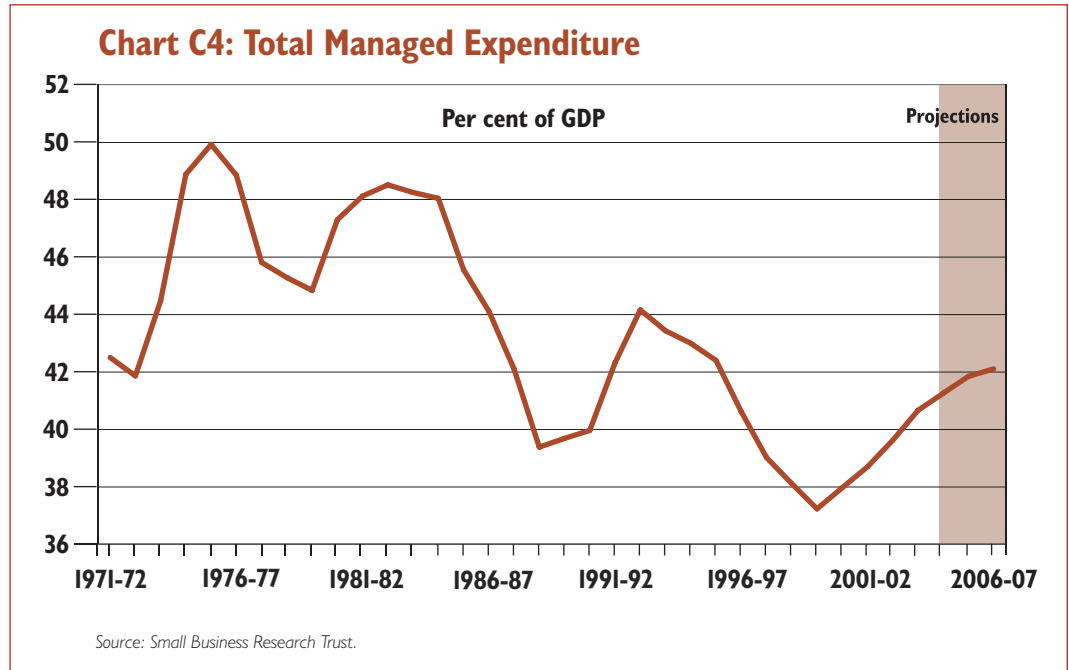
⁴ Excludes depreciation.

Table CI2: Changes to Total Managed Expenditure since the 2004 Pre-Budget Report

	£ billion				
	Outturn 2003-04	Estimate 2004-05	Projections		
			2005-06	2006-07	2007-08
Departmental Expenditure Limits					
Resource Budget	1.4	2.0	0.4	0.6	0.9
Capital Budget	0.2	-2.4	-0.4	0.5	0.3
Less depreciation	-0.3	-0.3	-0.1	0.0	0.0
Total Departmental Expenditure Limits	1.4	-0.7	-0.1	1.1	1.3
Annually Managed Expenditure					
Social security benefits	-4.3	0.2	0.9	0.4	0.1
Tax credits	1.5	0.3	0.3	0.3	0.7
Common Agricultural Policy	0.1	0.1	0.2	0.1	0.1
Net public sector pensions ¹	-0.3	-0.8	-0.3	-0.7	-0.9
National Lottery	0.0	0.0	0.0	0.0	0.0
Non-cash items in AME	0.1	-0.2	-0.6	0.4	0.9
Other departmental expenditure	-0.3	0.7	1.3	0.2	0.0
Net payments to EU institutions	0.0	1.7	0.1	-1.4	0.0
Locally-financed expenditure	-0.7	0.3	-0.2	-0.5	-0.9
Central government gross debt interest	0.0	0.0	0.4	0.4	0.6
Public corporations' own-financed capital expenditure	0.0	-0.1	0.0	0.2	0.2
AME margin	0.0	-1.0	-1.9	-0.4	0.3
Accounting adjustments ²	3.4	-1.7	-2.1	0.3	-1.6
Annually Managed Expenditure	-0.5	-0.4	-1.8	-0.8	-0.7
Total Managed Expenditure	0.9	-1.1	-1.9	0.3	0.6
<i>of which:</i>					
Public sector current expenditure	-0.2	2.5	-1.2	0.6	0.9
Public sector net investment	1.4	-3.4	-0.2	0.0	0.0
Public sector depreciation	-0.3	-0.3	-0.3	-0.3	-0.2

¹ Net public service pensions expenditure is reported on a national accounts basis.

² Accounting adjustments are net of depreciation and exclude FRS17 pension related items.



DEL and AME analysis

C66 Table C11 sets out projected spending on DEL and the main components of AME to the end of the 2004 Spending Review period in 2007-08. Table C12 shows change since the 2004 Pre-Budget Report.

DEL C67 As set out in Chapter 2, resource DEL spending for 2004-05 is higher than planned spending set out in the 2004 Pre-Budget Report, due to higher than expected expenditure to meet the UK's international commitments as well as use by departments of EYF to deliver key public service priorities, including health and education. Prior to 2004-05, drawdown of EYF has generally been more than offset by underspending. Higher spending on public services in 2004-05 reflects exceptional factors, including that planned expenditure growth in 2004-05 was lower than in both 2003-04 and 2005-06 and the use of EYF has enabled departments to smooth spending across the 2002 Spending Review period. Looking forward, planned expenditure growth slows after 2005-06 and departments therefore have an interest in maintaining reasonable contingency levels of EYF entitlements to allow sensible management of expenditure in the 2004 Spending Review period.

C68 The increase of £1.4 billion in resource DEL in 2003-04 since the 2004 Pre-Budget Report reflects the reclassification of expenditure on the Supporting People programme from AME to DEL. Apart from Budget policy decisions, the only overall changes to DEL for 2005-06 to 2007-08 since the 2004 Pre-Budget Report are reclassifications between DEL and AME, and some switches between resource and capital DEL. The changes include:

- switches of £0.2 billion in 2005-06 and 2006-07, and £0.1 billion in 2007-08 from resource to capital in ODPM DEL for realignment between direct investment and capital grants;
- a switch from Scottish Executive capital to resource DEL in 2005-06 of £0.2 billion and a switch of £0.1 billion from resource into capital in 2006-07 for realignment between direct investment and capital grants;
- switches of around £0.2 billion each year from ODPM AME to capital DEL for the funding of the Arms Length Management Organisation; and
- a switch of £0.5 billion from the Department of Health's DEL to their AME in 2005-06 for the capital spending of foundation hospitals.

C69 The detailed allocations of DELs are shown in Table C13. In line with previous practice, resource and capital DEL for 2004-05 includes an allowance for shortfall reflecting likely underspends against departmental provision.

AME C70 The main economic assumptions underpinning the AME projections are set out in Box C1 and Table C3. In particular it is assumed that the UK claimant count unemployment rises slowly to 0.89 million in 2007-08, from recent levels of 0.82 million. The AME total is also affected by the reclassifications described at the beginning of this section.

C71 Outturn for 2003-04 social security expenditure has decreased since the 2004 Pre-Budget Report by £4.3 billion. This is due to the reclassification of expenditure on the Supporting People programme as DEL, transferring £2.1 billion into the resource DEL total in this year. An additional £1.2 billion of the change is caused by revised estimates for child allowances in Income Support and Jobseeker's Allowance, which, from 2003-04, are paid as part of the Child Tax Credit and have been included in the tax credits line and excluded from the social security benefits line in order to give figures on a consistent definition over the forecast period. Forecasting changes in 2004-05, 2005-06 and 2007-08 have made only small differences since the 2004 Pre-Budget Report. Discretionary measures have increased the forecast by £0.8 billion in 2005-06, £0.2 billion in 2006-07 and £0.2 billion in 2007-08, as outlined in Chapter A.

C72 Forecast spending on the Child and Working Tax Credits differs from the 2004 Pre-Budget Report. Forecast costs have changed because of higher take up of the disabled elements of Child Tax Credit & Working Tax Credit and because of re-profiling of payment schedules. There have also been increases in tax credit payments scored as negative tax (see Table 7). Discretionary measures to increase the forecast by £0.3 billion in 2006-07 and £0.5 billion in 2007-08, as described in Chapter A.

C73 Forecast expenditure on the Common Agricultural Policy (CAP) has increased since the Pre-Budget Report. This is primarily because of revisions to the exchange rate assumption. However, in the national accounts, CAP payments are treated as a transaction between the EU and farmers and hence do not score in UK government expenditure – they are now removed in the accounting adjustments, and have no impact on Total Managed Expenditure (TME).

C74 Net public service pensions figures are reported on a national accounts basis. This spending is now expected to be lower than in the 2004 Pre-Budget Report. Current spending is lower by £0.8 billion in 2004-05, £0.3 billion in 2005-06, £0.7 billion in 2006-07 and £0.9 billion in 2007-08. This mainly reflects revisions to forecasts for the NHS pension scheme, in line with future workforce plans. There is increased capital spending of £0.2 billion in 2005-06.

Table CI3: Departmental Expenditure Limits – resource and capital budgets

	£ billion				
	Outturn 2003-04	Estimate 2004-05	Plans 2005-06	2006-07	2007-08
Resource Budget					
Education and Skills	23.1	24.6	26.3	28.1	29.6
Health	62.7	69.1	75.1	81.9	89.3
of which: NHS	60.9	66.9	72.8	79.9	87.3
Transport	7.8	8.3	8.8	10.8	9.9
Office of the Deputy Prime Minister	6.0	6.2	6.4	6.6	7.1
Local Government	40.9	43.4	46.2	48.8	51.3
Home Office	11.7	12.3	12.8	13.3	14.0
Departments for Constitutional Affairs	3.2	3.4	3.7	3.8	3.8
Attorney General's Departments	0.6	0.7	0.7	0.7	0.7
Defence	31.3	32.6	32.7	32.7	33.0
Foreign and Commonwealth Office	1.6	1.8	1.8	1.7	1.7
International Development	3.8	3.9	4.5	5.0	5.3
Trade and Industry	4.4	5.3	5.9	6.3	6.4
Environment, Food and Rural Affairs	2.7	3.2	3.1	3.3	3.4
Culture, Media and Sport	1.3	1.5	1.5	1.6	1.7
Work and Pensions	8.3	8.4	8.4	8.2	8.2
Scotland ¹	18.8	20.0	21.4	22.8	24.1
Wales ¹	9.8	10.7	11.3	12.1	12.8
Northern Ireland Executive ¹	6.4	7.0	7.3	7.7	8.0
Northern Ireland Office	1.0	1.2	1.2	1.1	1.1
Chancellor's Departments	4.5	5.0	5.2	5.2	5.2
Cabinet Office	1.9	2.0	2.0	2.0	2.1
Invest to Save Budget	0.0	0.0	0.0	0.0	0.0
Reserve	0.0	0.0	0.4	1.3	1.7
Unallocated special reserve ²	0.0	0.0	0.3	0.0	0.0
Allowance for shortfall ³	0.0	-1.8	0.0	0.0	2.0
Total Resource Budget DEL	251.9	268.7	286.9	304.8	320.6
Capital Budget					
Education and Skills	3.2	3.7	4.4	4.9	5.6
Health	2.5	3.1	3.8	5.3	6.3
of which: NHS	2.5	3.0	3.7	5.2	6.1
Transport	3.0	3.3	3.3	4.1	4.2
Office of the Deputy Prime Minister	2.6	2.9	3.0	2.9	2.9
Local Government	0.2	0.3	0.3	0.2	0.2
Home Office	0.9	1.1	1.2	1.2	1.3
Departments for Constitutional Affairs	0.1	0.2	0.1	0.1	0.1
Attorney General's Departments	0.0	0.0	0.0	0.0	0.0
Defence	6.1	6.6	6.9	7.0	7.6
Foreign and Commonwealth Office	0.0	0.1	0.1	0.1	0.1
International Development	0.0	0.0	0.0	0.0	0.0
Trade and Industry	0.6	0.2	0.3	0.5	0.5
Environment, Food and Rural Affairs	0.4	0.3	0.3	0.3	0.3
Culture, Media and Sport	0.1	0.2	0.1	0.1	0.1
Work and Pensions	0.2	0.3	0.3	0.2	0.1
Scotland ¹	1.4	2.0	1.9	2.1	2.2
Wales ¹	0.8	0.9	0.9	1.1	1.2
Northern Ireland Executive ¹	0.4	0.4	0.4	0.5	0.5
Northern Ireland Office	0.1	0.1	0.1	0.1	0.1
Chancellor's Departments	0.3	0.4	0.3	0.4	0.5
Cabinet Office	0.5	0.3	0.2	0.2	0.3
Invest to Save Budget	0.0	0.0	0.0	0.0	0.0
Reserve	0.0	0.0	0.5	0.6	1.1
Allowance for shortfall ³	0.0	-2.6	0.0	0.0	0.0
Total Capital Budget DEL	23.5	23.8	28.8	32.0	35.2
Depreciation	-9.4	-11.3	-11.8	-12.1	-11.8
Total Departmental Expenditure Limits	266.0	281.2	303.9	324.7	344.0
Total education spending	59.3	64.5	68.2	72.6	77.2

¹ For Scotland, Wales and Northern Ireland, the split between current and capital budgets is indicative and reflects the consequential of the application of the Barnett formula to planned changes in UK departments spending.

² This represents provision for the costs of military operations in Iraq and the UK's other international obligations. The figure for 2004-05 is after the further addition of £340 million announced in this Budget.

³ The allowance for shortfall reflects likely underspends in departmental forecasts.

AME C75 Changes to non-cash items in AME reflect revisions to the notional interest cost arising from unwinding the discount on public service pensions schemes liabilities, due to a change in the discount rate. The change to the discount rate reflects the requirements of FRS17 accounting treatment for pensions. Like all non-cash items, this does not score in TME and is removed in the accounting adjustments. Therefore these changes have no impact on TME.

C76 Other departmental expenditure has increased in 2004-05, 2005-06 and 2006-07. This reflects increased estimates for Department of Health PFI pilot projects and departmental lending to public corporations. Both of these items are classified as financial transactions and are removed from TME in the accounting adjustments. In 2005-06, there is also an increase associated with the NNDR outturn adjustment and with capital spending of NHS foundation trusts. The latter is a switch into AME from DEL as described at the beginning of this section, so again has no impact on TME.

C77 The net payments to EU institutions forecast reflects revised estimates of EU receipts. It also takes account of more recent information on the EU Budget than was available at the time of the 2004 Pre-Budget Report and of changes in the timing of certain payments to the EU Budget. As described above, Common Agricultural Policy (CAP) payments are treated as a transaction between the EU and farmers and hence do not score in UK government expenditure. Therefore the EU receipts associated with this expenditure are now also removed in the accounting adjustments and do not score in TME. The overall effect of changes to net payments to the EU on the current budget since the 2004 Pre-Budget Report is to reduce the current budget by about £1 billion in 2004-05 and increase it by around £1 billion in 2005-06, mainly because of changes to the timing of Structural Funds receipts. There are only small changes in later years.

C78 Changes to local authority self-financed expenditure (LASFE) reflect the revision of the forecasting assumption made for increases in Council Tax. This is outlined in more detail in the Tax-by-tax analysis sub-section. In 2006-07 and 2007-08 payments are higher mainly because of the cumulative effects of higher cash requirement.

C79 Central government debt interest payments for 2005-06 are higher than at the 2004 Pre-Budget Report, largely as a result of the impact of higher Retail Price Index (RPI) on index linked gilt payments.

C80 The main accounting adjustments, which reconcile the DEL and AME measures of spending with the national accounts measure, are shown in Table C14. Changes to the accounting adjustments since the last forecast are mainly due to:

- reductions in depreciation due to the revised recording of road maintenance and repair expenditure; and
- the removal of CAP expenditure and the associated receipts from the EC.

Table C14: Accounting adjustments

	£ billion				
	Outturn	Estimate	Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
Tax credits for individuals	0.1	0.0	0.0	0.0	0.0
European Union contributions	-4.7	-4.0	-3.9	-4.0	-4.0
Other central government programmes	0.9	0.9	0.8	0.8	0.7
VAT refunds	9.1	10.0	10.7	11.8	12.6
Central government non-trading capital consumption	5.3	5.5	5.9	6.3	6.7
Non-cash items in resource budgets and not in TME	-12.3	-10.5	-10.1	-12.6	-14.3
Expenditure financed by revenue receipts	0.2	0.3	0.3	0.3	0.3
Local authorities	4.5	3.1	5.0	6.3	6.3
General government consolidation	-5.2	-5.0	-5.0	-5.1	-5.3
Public corporations	0.1	0.2	0.2	0.3	0.3
Financial transactions	0.8	-1.0	0.1	0.4	0.4
Other accounting adjustments	0.1	-0.7	-1.7	0.9	-0.2
Total accounting adjustments	-1.3	-1.2	2.3	5.1	3.6

C81 Table C15 shows public sector capital expenditure from 2003-04 to 2007-08.

Table C15: Public sector capital expenditure

	£ billion				
	Outturn	Estimate	Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
Capital Budget DEL	23.5	23.8	28.8	32.0	35.2
Locally-financed expenditure	-0.6	2.1	2.2	2.3	2.4
National Lottery	1.2	0.9	0.9	0.8	0.7
Public corporations' own-financed capital expenditure	2.5	2.2	2.3	2.3	2.5
Other capital spending in AME	2.5	3.9	7.5	8.1	7.5
AME margin	0.0	0.0	0.1	0.2	0.3
Public sector gross investment¹	29.0	33.0	41.7	45.8	48.6
Less depreciation	14.0	14.6	15.5	16.4	17.4
Public sector net investment	15.0	18.3	26.2	29.4	31.1
Proceeds from the sale of fixed assets ²	6.7	5.8	5.2	5.0	4.9

¹ This and previous lines are all net of sales of fixed assets.

² Projections of total receipts from the sale of fixed assets by public sector.

C82 Table C16 shows estimated receipts from loans and sales of assets from 2003-04 to 2007-08.

Table C16: Loans and sales of assets

	£ billion				
	Outturn	Estimate	Projections		
	2003-04	2004-05	2005-06	2006-07	2007-08
Sales of fixed assets					
Central government	1.1	1.0	1.0	1.0	1.0
Local authorities	5.6	4.8	4.2	4.0	3.9
Total sales of fixed assets	6.7	5.8	5.2	5.0	4.9
Total loans and sales of financial assets	-2.1	-2.2	-2.4	-2.7	-3.4
Total loans and sales of assets	4.6	3.7	2.8	2.3	1.5

PRIVATE FINANCE INITIATIVE

C83 Under the Private Finance Initiative (PFI) the public sector contracts to purchase services on a long-term basis so as to take advantage of private sector management skills incentivised by having private finance at risk. The private sector has always been involved in the building and maintenance of public infrastructure, but PFI ensures that contractors are bound into long-term maintenance contracts and shoulder responsibility for the quality of the work they do. With PFI, the public sector defines what is required to meet public needs and ensures delivery of the outputs through the contract. Consequently, the private sector can be harnessed to deliver investment in better quality public services whilst frontline services are retained within the public sector.

C84 The Government only uses PFI where it is appropriate and where it expects it to deliver value for money. This is based on an assessment of the lifetime costs of both providing and maintaining the underlying asset, and of the running costs of delivering the required level of service. In assessing where PFI is appropriate, the Government's approach is based on its commitment to efficiency, equity and accountability, and on the Prime Minister's principles of public service reform. PFI is only used where it can meet these requirements, and where the value for money it offers is not at the expense of the terms and conditions of staff. The Government is committed to securing the best value for its investment programme by ensuring that there is no inherent bias in favour of one procurement option over another.

C85 Table C17 shows a breakdown by department of the estimated capital investment in public services resulting from signed PFI contracts. Table C18 shows the estimated total capital value of contracts that are at preferred bidder stage and are expected to reach financial close within the next three years. Under PFI, the public sector contracts for services, including the availability and management of facilities, and not assets. Capital investment is only one of the activities undertaken by the private sector in order to supply these services. The figures in Tables C17 and C18 report the capital value of projects in order to show investment on a basis comparable with conventional capital procurement.

C86 Table C19 shows a forecast of the estimated payments for services flowing from signed PFI projects. Actual expenditure will depend on the details of the payment mechanism for each contract. Payments may be lower than those estimated as a result of deductions that can be applied if the supplier fails to meet required performance standards. Variances may also occur as a result of agreed changes to the service requirements that are made during the course of the contract, or because of contractual arrangements that trigger compensation on termination. The fact that capital investment only represents one element of the overall contract means that the figures presented in this table should not be taken to be directly comparable with a public sector debt liability.

Table C17: Departmental estimate of capital spending by the private sector (signed deals)^{1,2}

	£ million		
	Projections		
	2005-06	2006-07	2007-08
Education and Skills ³			
Health	848	560	334
Transport ⁴	1494	1343	1202
Office of the Deputy Prime Minister	71	53	14
Home Office	45	0	0
Constitutional Affairs	27	18	0
Defence	458	304	181
Foreign and Commonwealth Office	5	5	0
Trade and Industry	8	1	0
Environment, Food and Rural Affairs	47	28	27
Work and Pensions			
Scotland	109	32	
Wales	23	0	0
Northern Ireland Executive	40	24	0
Chancellor's Departments	41	36	37
Cabinet Office			
Culture, Media and Sports	13	9	0
Total	3229	2413	1795

¹ Investment in assets scored on the public sector balance sheet also score as public sector net investment.

² PFI activity in local authority projects is included under the sponsoring central government department.

³ Excludes private finance activity in educational institutions classified to the private sector.

⁴ Includes estimates of the capital expenditure for the London Underground Limited Public Private Partnership PFI Contracts in the years that investments are expected to take place.

Table CI8: Estimated aggregated capital value of projects at preferred bidder stage

	£ million		
	Projections		
	2005-06	2006-07	2007-08
Education and Skills	290	0	0
Health	3039	0	0
Transport	248	0	0
Office of the Deputy Prime Minister	135	0	0
Home Office	0	0	0
Constitutional Affairs	0	0	0
Defence	1418	0	0
Foreign and Commonwealth Office	0	0	0
Trade and Industry	0	0	0
Environment, Food and Rural Affairs	0	0	0
Work and Pensions	0	0	0
Scotland	150	0	0
Wales	93	0	0
Northern Ireland Executive	51	0	0
Chancellor's Departments	0	0	0
Cabinet Office	0	0	0
Culture, Media and Sport	42	0	0
Total	5280	0	0

¹ The figures reported in this table reflect the fact that, at the time of collection, all projects that are at preferred bidder are expected to reach financial close before the end of 2005-06.

Table CI9: Estimated payments under PFI contracts – March 2005 (signed deals)¹

	£ billion			
	Projections			
2005-06	6.4	2018-19	4.3	
2006-07	6.8	2019-20	4.3	
2007-08	6.9	2020-21	4.4	
2008-09	6.8	2021-22	4.1	
2009-10	6.9	2022-23	4.1	
2010-11	6.9	2023-24	4.1	
2011-12	6.9	2024-25	4.1	
2012-13	6.9	2025-26	4.1	
2013-14	7	2026-27	3.8	
2014-15	7	2027-28	3.6	
2015-16	7	2028-29	3.3	
2016-17	7.1	2029-30	3	
2017-18	6.5	2030-31	2.1	

¹ The figures between 2004-05 and 2017-18 include estimated payments for the LUL PPP contracts. These contracts contain periodic reviews each 7.5 years and therefore the service payments are not fixed after 2009-10.

FINANCING REQUIREMENT

C87 Table C20 presents projections of the net cash requirement by sector, giving details of financial transactions that do not affect net borrowing (the change in the sector's net financial indebtedness) but do affect its financing requirement.

C88 Although public sector net borrowing is slightly lower in 2005-06 than in the PBR, the cash requirement has increased because of higher net lending to the private sector and higher accruals adjustments, largely reflecting changes to the timing of cash receipts from the EU.

Table C20: Public sector net cash requirement

	£ billion								
	2004-05				2005-06				
	General government			Public sector	General government				Public sector
Central government	Local authorities	Public corporations	Central government		Local authorities	Public corporations	Public sector		
Net borrowing	37.0	-2.8	0.2	34.4	34.2	-2.2	-0.1	31.9	
<i>Financial transactions</i>									
Net lending to private sector and abroad	2.0	0.1	0.0	2.1	2.3	0.1	0.0	2.4	
Cash expenditure on company securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Accounts receivable/payable	4.0	0.0	-0.9	3.1	3.9	0.0	-0.7	3.1	
Adjustment for interest on gilts	-2.4	0.0	0.0	-2.4	-2.6	0.0	0.0	-2.6	
Miscellaneous financial transactions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Own account net cash requirement	40.7	-2.7	-0.7	37.3	37.7	-2.1	-0.9	34.8	
Net lending within the public sector	2.1	-1.6	-0.5	0.0	2.4	-1.5	-0.9	0.0	
Net cash requirement¹	42.9	-4.3	-1.3	37.3	40.2	-3.6	-1.8	34.8	

¹ Market and overseas borrowing for local government and public corporation sectors.

C89 Table C21 updates the financing arithmetic for both 2004-05 and 2005-06 in line with the new public finances forecast. The forecast for the central government net cash requirement (CGNCR) for 2004-05 is £42.9 billion, an increase of £3.2 billion from the 2004 Pre-Budget Report forecast of £39.7 billion. Allowing for a £0.1 billion increase in financing due to the Debt Management Office's (DMO's) secondary market purchases of gilts means that the net financing requirement for 2004-05 is now expected to be £55.7 billion, an increase of £3.3 billion from the 2004 Pre-Budget Report forecast of £52.4 billion. This increased financing requirement is being met by a £2.0 billion increase in the forecast stock of Treasury bills, resulting in a £1.3 billion reduction in the forecast level of DMO's short-term cash position at end March 2005.

C90 The forecast for the CGNCR for 2005-06 is £40.2 billion. Gross gilt redemptions are £14.5 billion and National Savings & Investments net contribution to financing is estimated to be £3.5 billion. This means that the net financing requirement for 2005-06 is forecast to be £51.2 billion. The DMO will aim to meet the net financing requirement by:

- gross gilts issuance of £53.5 billion;
- a reduction in the Treasury bill stock of £1.0 billion by end March 2006; and
- a £1.3 billion reduction in the DMO's short-term cash position by end March 2006.

C91 At the Pre-Budget Report 2004, the Government instructed the DMO formally to consult the market about possible issuance of ultra-long (circa 50-year maturity) conventional and index-linked gilts, perhaps in the alternative format of fixed-term annuities. A full summary of the responses to the consultation is available on the DMO's website at www.dmo.gov.uk.

C92 The key conclusions from the consultation are that:

- from 2005-06, the DMO may issue conventional and index-linked gilts with maturities of up to approximately 50-years; and
- the DMO will not issue conventional or index-linked gilts in annuity format in 2005-06.

C93 Full details of the DMO's financing remit including the structure of gilts issuance and the gilt auction calendar for 2005-06 can be found in the Debt and Reserves Management Report 2005-06 which is published today.

Table C21: Financing requirement forecast

	£ billion			
	2004-05		2005-06	
	April 2004 Revised Remit ¹	December 2004 Pre-Budget Report	March 2005 Budget	March 2005 Budget
Central Government net cash requirement	35.6	39.7	42.9	40.2
Gilt Redemptions	14.7	14.7	14.7	14.5
Net financing of the Official Reserves	0.0	0.0	0.0	0.0
Debt buy-backs	0.0	0.0	0.1	0.0
Gross financing requirement	50.3	54.4	57.7	54.7
Less assumed net contribution from National Savings & Investments	2.0	2.0	2.0	3.5
Net financing requirement	48.3	52.4	55.7	51.2
<i>Financed by:</i>				
1. Debt Issuance by the DMO				
a) Change in the Treasury bill stock	-1.8	-0.8	1.2	-1.0
b) Gross gilt sales	47.1	50.3	50.3	53.5
2. Planned changes in Government's short-term cash position²	2.9	2.9	4.2	-1.3
3. Unanticipated changes in short-term debt	-	-	-1.3	-

Note: Figures may not sum due to rounding.

¹Budget 2004 financing arithmetic was revised on 22 April 2004 to reflect outturn data for 2003-04.

²Including changes in the DMO's cash deposit at the Bank of England.

ANALYSIS BY SUBSECTOR AND ECONOMIC CATEGORY

C94 Table C22 shows a breakdown of general government transactions by economic category for 2003-04 to 2006-07. Table C23 shows a more detailed breakdown for public sector transactions by sub-sector and economic category for each of these years.

C95 The allocation of public sector transactions between sub-sectors has changed since the 2004 Pre-Budget Report, largely because of better data on the split of TME. This has the effect of substantially increasing central government net borrowing, and hence the cash requirement, and reducing Local Authority counterparts.

Table C22: General government transactions by economic category

	£ billion				
	Estimate 2003-04	Projections 2004-05	2005-06	2006-07	2007-08
<i>Current receipts</i>					
Taxes on income and wealth	145.7	163.4	183.9	200.6	215.4
Taxes on production and imports	148.7	155.9	163.7	172.4	180.9
Other current taxes	23.3	24.0	25.4	27.2	29.2
Taxes on capital	2.5	2.9	3.4	3.6	3.8
National insurance contributions	75.1	78.3	83.1	87.7	93.4
Gross operating surplus	10.1	10.7	11.6	12.5	13.4
Rent and other current transfers	1.6	1.6	1.6	1.7	1.7
Interest and dividends from private sector and abroad	3.8	4.4	4.3	4.5	4.6
Interest and dividends from public sector	5.8	6.3	6.9	7.4	7.6
Total current receipts	416.6	447.4	483.8	517.6	550.1
<i>Current expenditure</i>					
Current expenditure on goods and services	233.0	247.9	261.9	279.9	297.1
Subsidies	7.2	6.2	6.3	7.0	6.7
Net social benefits	135.1	143.2	150.0	151.1	158.1
Net current grants abroad	-0.9	0.0	0.7	0.3	-0.3
Other current grants	28.1	29.3	30.9	35.4	37.9
Interest and dividends paid	22.6	24.3	25.9	27.6	28.9
AME margin	0.0	0.0	0.9	1.8	2.7
Total current expenditure	425.1	450.9	476.7	503.1	531.1
Depreciation	10.1	10.7	11.6	12.5	13.4
Surplus on current budget	-18.7	-14.2	-4.4	2.0	5.5
<i>Capital expenditure</i>					
Gross domestic fixed capital formation	18.0	20.1	26.7	30.9	33.4
Less depreciation	-10.1	-10.7	-11.6	-12.5	-13.4
Increase in inventories	0.0	0.3	0.2	0.2	0.1
Capital grants (net) within public sector	1.2	0.7	0.9	0.4	0.4
Capital grants to private sector	8.9	11.1	13.4	13.6	13.5
Capital grants from private sector	-1.3	-1.6	-2.0	-2.0	-1.9
AME margin	0.0	0.0	0.1	0.2	0.3
Net investment	16.7	20.0	27.6	30.7	32.3
Net borrowing¹	35.4	34.2	32.0	28.7	26.8
<i>of which:</i>					
Central government net borrowing	37.3	37.0	34.2	29.5	27.9
Local authority net borrowing	-2.0	-2.8	-2.1	-0.8	-1.1
Gross debt (Maastricht basis)					
Central government	387.9	432.5	475.4	510.4	545.8
Local government	53.3	49.0	45.5	43.4	40.8

¹ Although this is based on the ESA95 definition of general government net borrowing (GGNB), the projections are identical to GGNB calculated on a Maastricht definition.

Table C23: Public sector transactions by sub-sector and economic category

	£ billion			
	2003-04			
	General government			Public sector
	Central government	Local authorities	Public corporations	
<i>Current receipts</i>				
Taxes on income and wealth	145.7	0.0	-0.1	145.6
Taxes on production and imports	148.6	0.1	0.0	148.7
Other current taxes	5.1	18.2	0.0	23.2
Taxes on capital	2.5	0.0	0.0	2.5
National insurance contributions	75.1	0.0	0.0	75.1
Gross operating surplus	5.3	4.9	7.6	17.8
Rent and other current transfers	1.6	0.0	0.0	1.6
Interest and dividends from private sector and abroad	3.1	0.7	0.6	4.4
Interest and dividends from public sector	4.8	1.0	-5.8	0.0
Total current receipts	391.6	24.9	2.4	418.9
<i>Current expenditure</i>				
Current expenditure on goods and services	141.4	91.6	0.0	233.0
Subsidies	6.0	1.2	0.0	7.2
Net social benefits	121.7	13.4	0.0	135.1
Net current grants abroad	-0.9	0.0	0.0	-0.9
Current grants (net) within public sector	86.8	-86.8	0.0	0.0
Other current grants	28.1	0.0	0.0	28.1
Interest and dividends paid	22.2	0.4	0.2	22.8
AME margin	0.0	0.0	0.0	0.0
Total current expenditure	405.4	19.7	0.2	425.3
Depreciation	5.3	4.9	3.9	14.0
Surplus on current budget	-19.0	0.3	-1.8	-20.4
<i>Capital expenditure</i>				
Gross domestic fixed capital formation	8.9	9.0	3.1	21.0
Less depreciation	-5.3	-4.9	-3.9	-14.0
Increase in inventories	0.0	0.0	0.0	0.1
Capital grants (net) within public sector	7.2	-6.0	-1.2	0.0
Capital grants to private sector	7.8	1.1	0.3	9.2
Capital grants from private sector	-0.4	-0.9	0.0	-1.3
AME margin	0.0	0.0	0.0	0.0
Net investment	18.4	-1.6	-1.7	15.0
Net borrowing	37.3	-2.0	0.0	35.4

Table C23: Public sector transactions by sub-sector and economic category

£ billion				
2004-05				
	General government			Public sector
	Central government	Local authorities	Public corporations	
<i>Current receipts</i>				
Taxes on income and wealth	163.4	0.0	-0.1	163.3
Taxes on production and imports	155.7	0.2	0.0	155.9
Other current taxes	5.1	19.0	0.0	24.0
Taxes on capital	2.9	0.0	0.0	2.9
National insurance contributions	78.3	0.0	0.0	78.3
Gross operating surplus	5.5	5.2	8.0	18.7
Rent and other current transfers	1.6	0.0	0.0	1.6
Interest and dividends from private sector and abroad	3.5	0.9	0.6	5.0
Interest and dividends from public sector	3.6	2.7	-6.3	0.0
Total current receipts	419.5	27.9	2.3	449.7
<i>Current expenditure</i>				
Current expenditure on goods and services	150.7	97.3	0.0	247.9
Subsidies	4.9	1.3	0.0	6.2
Net social benefits	128.1	15.1	0.0	143.2
Net current grants abroad	0.0	0.0	0.0	0.0
Current grants (net) within public sector	93.1	-93.1	0.0	0.0
Other current grants	29.2	0.0	0.0	29.3
Interest and dividends paid	23.8	0.4	0.2	24.4
AME margin	0.0	0.0	0.0	0.0
Total current expenditure	430.0	21.0	0.2	451.1
Depreciation	5.5	5.2	4.0	14.6
Surplus on current budget	-16.0	1.7	-1.8	-16.1
<i>Capital expenditure</i>				
Gross domestic fixed capital formation	9.3	10.8	2.7	22.8
Less depreciation	-5.5	-5.2	-4.0	-14.6
Increase in inventories	0.3	0.0	0.0	0.3
Capital grants (net) within public sector	7.8	-7.0	-0.7	0.0
Capital grants to private sector	10.0	1.2	0.3	11.4
Capital grants from private sector	-0.7	-0.9	0.0	-1.6
AME margin	0.0	0.0	0.0	0.0
Net investment	21.0	-1.1	-1.7	18.3
Net borrowing	37.0	-2.8	0.2	34.4

Table C23: Public sector transactions by sub-sector and economic category

	£ billion			
	2005-06			
	General government			Public sector
	Central government	Local authorities	Public corporations	
<i>Current receipts</i>				
Taxes on income and wealth	183.9	0.0	-0.1	183.8
Taxes on production and imports	163.5	0.2	0.0	163.7
Other current taxes	5.4	20.0	0.0	25.4
Taxes on capital	3.4	0.0	0.0	3.4
National insurance contributions	83.1	0.0	0.0	83.1
Gross operating surplus	5.9	5.7	9.1	20.7
Rent and other current transfers	1.6	0.0	0.0	1.6
Interest and dividends from private sector and abroad	3.6	0.7	0.6	4.9
Interest and dividends from public sector	3.2	3.7	-6.9	0.0
Total current receipts	453.6	30.2	2.8	486.7
<i>Current expenditure</i>				
Current expenditure on goods and services	159.2	102.8	0.0	261.9
Subsidies	4.9	1.4	0.0	6.3
Net social benefits	134.1	15.9	0.0	150.0
Net current grants abroad	0.7	0.0	0.0	0.7
Current grants (net) within public sector	98.1	-98.1	0.0	0.0
Other current grants	30.9	0.0	0.0	30.9
Interest and dividends paid	25.6	0.4	0.2	26.2
AME margin	0.9	0.0	0.0	0.9
Total current expenditure	454.3	22.3	0.2	476.9
Depreciation	5.9	5.7	3.9	15.5
Surplus on current budget	-6.6	2.2	-1.3	-5.7
<i>Capital expenditure</i>				
Gross domestic fixed capital formation	12.0	14.7	3.0	29.7
Less depreciation	-5.9	-5.7	-3.9	-15.5
Increase in inventories	0.2	0.0	0.0	0.2
Capital grants (net) within public sector	10.2	-9.3	-0.9	0.0
Capital grants to private sector	11.8	1.6	0.3	13.7
Capital grants from private sector	-0.9	-1.2	0.0	-2.0
AME margin	0.1	0.0	0.0	0.1
Net investment	27.6	0.0	-1.4	26.2
Net borrowing	34.2	-2.1	-0.1	31.9

Table C24: Historical series of public sector balances, receipts and debt

Per cent of GDP									
	Public sector current budget	Cyclically-adjusted surplus on current budget	Public sector net borrowing	Cyclically-adjusted public sector net borrowing	Public sector net cash requirement	Net taxes and social security contributions	Public sector current receipts	Public sector net debt ¹	Public sector net worth ²
1970-71	6.7		-0.6		1.2		43.3		
1971-72	4.2		1.1		1.4		41.4		
1972-73	2.0	2.5	2.8	2.3	3.6		39.0		
1973-74	0.3	-0.8	4.9	6.0	5.9		39.6		
1974-75	-1.1	-2.4	6.6	7.9	9.0		42.3	52.1	
1975-76	-1.6	-1.5	7.0	7.0	9.3		42.9	53.8	
1976-77	-1.2	-0.3	5.5	4.6	6.4		43.3	52.3	
1977-78	-1.4	-1.0	4.3	3.8	3.7		41.5	49.0	
1978-79	-2.6	-2.5	5.0	4.9	5.2	33.5	40.2	47.1	
1979-80	-1.9	-1.8	4.1	4.0	4.7	33.9	40.7	43.9	
1980-81	-3.0	-1.6	4.9	3.4	5.2	35.9	42.4	46.0	
1981-82	-1.4	2.4	2.3	-1.5	3.3	38.6	45.8	46.2	
1982-83	-1.5	2.8	3.0	-1.3	3.2	38.7	45.5	44.8	
1983-84	-2.0	1.7	3.8	0.1	3.2	38.2	44.4	45.1	
1984-85	-2.2	0.8	3.7	0.7	3.1	38.9	44.3	45.3	
1985-86	-1.2	0.6	2.4	0.6	1.6	38.1	43.2	43.5	
1986-87	-1.4	-1.2	2.1	1.9	0.9	37.8	42.0	41.0	
1987-88	-0.3	-1.6	1.0	2.2	-0.7	37.6	41.1	36.8	74.1
1988-89	1.7	-0.9	-1.3	1.3	-3.0	36.9	40.7	30.5	79.1
1989-90	1.4	-1.4	-0.2	2.6	-1.3	36.2	39.9	27.7	70.9
1990-91	0.4	-1.2	1.0	2.6	-0.1	35.9	38.9	26.2	60.4
1991-92	-2.0	-1.5	3.8	3.3	2.3	34.7	38.5	27.4	53.1
1992-93	-5.6	-3.6	7.6	5.6	5.9	33.7	36.6	32.0	40.3
1993-94	-6.2	-4.0	7.8	5.5	7.1	32.8	35.6	37.2	28.5
1994-95	-4.8	-3.4	6.3	4.8	5.3	34.0	36.7	40.8	27.6
1995-96	-3.4	-2.6	4.8	4.0	4.3	34.7	37.6	42.7	19.8
1996-97	-2.8	-2.3	3.5	3.0	2.9	34.8	37.1	43.6	16.1
1997-98	-0.2	-0.1	0.8	0.7	0.2	36.0	38.2	41.6	12.6
1998-99	1.2	0.8	-0.4	-0.1	-0.8	36.5	38.5	39.1	11.3
1999-00	2.2	1.8	-1.7	-1.4	-0.9	36.5	38.8	36.3	14.2
2000-01	2.2	1.6	-1.6	-1.0	-3.9	37.4	39.5	31.3	19.1
2001-02	1.0	0.7	0.0	0.2	0.3	36.8	38.6	30.2	24.0
2002-03	-1.3	-0.7	2.4	1.8	2.3	35.4	37.1	31.5	23.8
2003-04	-1.8	-1.0	3.2	2.3	3.5	35.6	37.5	32.8	24.7

¹ At end-March; GDP centred on end-March.

² At end-December; GDP centred on end-December.

Table C25: Historical series of government expenditure

	£ billion (2003–04 prices)				Per cent of GDP			
	Public sector current expenditure	Public sector net investment	Public sector gross investment ¹	Total managed expenditure	Public sector current expenditure	Public sector net investment	Public sector gross investment ¹	Total managed expenditure
1970-71	170.2	31.9	52.3	222.5	32.6	6.1	10.0	42.7
1971-72	178.2	28.2	49.1	227.3	33.3	5.3	9.2	42.5
1972-73	185.9	27.1	48.9	234.9	33.1	4.8	8.7	41.9
1973-74	204.1	30.4	54.9	258.9	35.1	5.2	9.4	44.5
1974-75	226.3	32.2	58.5	284.8	38.8	5.5	10.0	48.9
1975-76	231.4	31.6	58.2	289.5	39.9	5.5	10.0	49.9
1976-77	238.2	25.9	53.3	291.6	39.9	4.3	8.9	48.8
1977-78	234.6	17.5	45.0	279.7	38.4	2.9	7.4	45.8
1978-79	241.7	15.3	43.4	285.0	38.4	2.4	6.9	45.3
1979-80	247.7	14.2	42.7	290.4	38.2	2.2	6.6	44.8
1980-81	255.0	11.4	40.2	295.2	40.8	1.8	6.4	47.3
1981-82	266.6	5.8	34.5	301.1	42.6	0.9	5.5	48.1
1982-83	272.4	9.6	37.4	309.8	42.7	1.5	5.9	48.5
1983-84	280.8	11.8	39.5	320.3	42.3	1.8	5.9	48.2
1984-85	288.6	10.4	36.7	325.2	42.6	1.5	5.4	48.0
1985-86	288.5	8.8	32.2	320.7	41.0	1.2	4.6	45.6
1986-87	293.3	5.2	29.0	322.3	40.1	0.7	4.0	44.1
1987-88	296.5	5.1	27.0	323.5	38.6	0.7	3.5	42.1
1988-89	289.4	2.9	25.5	314.9	36.2	0.4	3.2	39.4
1989-90	291.8	9.8	32.6	324.4	35.7	1.2	4.0	39.7
1990-91	293.3	11.8	31.6	324.9	36.1	1.4	3.9	40.0
1991-92	310.6	14.9	31.7	342.4	38.4	1.8	3.9	42.3
1992-93	325.8	16.2	32.0	357.7	40.2	2.0	3.9	44.2
1993-94	335.2	13.1	28.7	363.8	40.0	1.6	3.4	43.4
1994-95	346.1	12.7	28.9	375.1	39.7	1.5	3.3	43.0
1995-96	351.1	12.2	28.6	379.7	39.2	1.4	3.2	42.4
1996-97	352.3	6.6	21.2	373.5	38.3	0.7	2.3	40.6
1997-98	352.0	6.0	20.3	372.2	36.9	0.6	2.1	39.0
1998-99	351.0	7.7	21.6	373.1	35.9	0.8	2.2	38.1
1999-00	357.2	5.4	19.7	377.4	35.2	0.5	1.9	37.2
2000-01	377.3	6.1	20.4	398.1	36.0	0.6	1.9	38.0
2001-02	387.6	10.9	25.2	413.2	36.3	1.0	2.4	38.7
2002-03	403.5	12.0	26.2	430.2	37.1	1.1	2.4	39.6
2003-04	425.3	15.0	29.0	454.7	38.1	1.3	2.6	40.7

¹ Net of sales of fixed assets.

CONVENTIONS USED IN PRESENTING THE PUBLIC FINANCES

FORMAT FOR THE PUBLIC FINANCES

The June 1998 Economic and Fiscal Strategy Report (EFSR), set out a new format for presenting the public finances that corresponded more closely to the two fiscal rules. The three principal measures are:

- the surplus on the current budget (relevant to the golden rule);
- public sector net borrowing; and
- the public sector net debt ratio (relevant to the sustainable investment rule).

These measures are based on the national accounts and are consistent with the European System of Accounts 1995 (ESA95). Estimates and forecasts of the public sector net cash requirement (formerly called the public sector borrowing requirement) are still shown in the FSBR, but they are given less prominence.

The fiscal rules are similar to the criteria for deficits and debt laid down in the Treaty but there are important definitional differences:

- UK fiscal rules cover the whole public sector, whereas the Treaty deficit and debt only includes general (i.e. central and local) government;
- The fiscal rules apply over the whole economic cycle, not year to year;
- The current budget excludes capital spending, which is included in the Treaty deficit measure; and
- The UK debt measure is net of liquid assets, whereas the Treaty measure uses gross debt.

From February 2000 the Treaty deficit moved to being reported on an ESA95 basis.

NATIONAL ACCOUNTS

The **national accounts** record most transactions, including most taxes (although not corporation tax, self-assessment income tax and some other Inland Revenue taxes which, because of practical difficulties, are scored on a cash basis) on an accruals basis, and impute the value of some transactions where no money changes hands (for example, non-trading capital consumption).

Full details of the sources for each table are included in the Budget 2005 technical annex: data sources, economy forecasts and charts, available on the Treasury's internet site and on request from the Treasury's Public Enquiry Unit (020 7270 4558).

The **outturn** figures are based on series published in the monthly Public Sector Finance release (last published in February 2005). The figures are also adjusted to take account of the changes announced by ONS, where the size of the change has also been publicly announced. This includes the reviews concerning roads maintenance expenditure detailed in ONS's Technical Explanatory Note published on 28 February 2005.

The principal measures drawn from the national accounts are described below.

FISCAL AGGREGATES

The **current budget** (formerly known as the current balance) measures the balance of current account revenue over current expenditure (including depreciation). The definition of the current budget presented in this chapter is very similar to the National Accounts concept of net saving. It differs only in that it includes taxes on capital (mainly inheritance tax) in current rather than capital receipts. The current budget is used to measure progress against the golden rule. The actual measure is the average surplus on the current budget expressed as a ratio to GDP over the economic cycle.

Public sector **net borrowing** (formerly known as the financial deficit in the UK National Accounts) is the balance between expenditure and income in the consolidated current and capital accounts. It differs from the public sector net cash requirement in that it is measured on an accruals basis and because certain fiscal transactions (notable net lending and net acquisition of other financial assets, which affect the level of borrowing but not the public sector's net financial indebtedness) are excluded from public sector net borrowing but included in the public sector net cash requirement.

Public sector net debt is approximately the stock analogue of the public sector net cash requirement. It measures the public sector's financial liabilities to the private sector and abroad, net of short-term financial assets such as bank deposits and foreign exchange reserves.

General government gross debt, the Treaty debt ratio, is the measure of debt used in the European Union's Excessive Deficit Procedure. As a general government measure, it excludes the debt of public corporations. It measures general government's total financial liabilities before netting off short-term financial assets.

Public sector net worth represents the public sector's overall net balance sheet position. It is equal to the sum of the public sector's financial and non-financial assets less its total financial liabilities. The estimates of tangible assets are subject to wide margins of error, because they depend on broad assumptions, for example about asset lives, which may not be appropriate in all cases. The introduction of resource accounting for central government departments will lead in time to an improvement in data quality, as audited information compiled from detailed asset registers becomes available.

PUBLIC SECTOR RECEIPTS

Net taxes and national insurance contributions (NTNIC) is a measure of net cash payments made to UK government and differs in several respects from the national accounts measure of total public sector current receipts (PSCR). A reconciliation between the two aggregates is given in the lower half of Table C8. The main adjustments are:

- accruals adjustments, mainly on income tax, national insurance contributions and VAT, are added to change the basis of figures from cash to national accounts accruals;
- some tax payments that are collected by the Government, but then paid to the EU, are subtracted as they do not score as government receipts in the national accounts;
- tax paid by public corporations is also subtracted, as it has no impact on overall public sector receipts;

- an adjustment is made for tax credits. In NTNIC, all tax credits are scored as negative tax to the extent that they are less equal to the tax liability of the household, and as public expenditure where they exceed the liability, in line with the Organisation for Economic Cooperation and Development (OECD) Revenue Statistics guidelines. Although the ONS have adopted this treatment for the Working Tax Credit and Child Tax Credit, which were introduced in April 2003, they have continued to treat the Working Families' Tax Credit (WFTC), the Disabled Person's Tax Credit (DPTC) and enhanced and payable company tax credits entirely as public expenditure in the national accounts. Those parts of WFTC, DPTC and company tax credits that offset tax liability in NTNIC are added back into current receipts in Table C8;
- interest and other non-tax receipts, which are excluded from NTNIC, are added. This excludes oil royalties, as they are already included in NTNIC, even though the national accounts treat them as non-tax receipts; and
- business rates paid by local authorities are included in the calculation of NTNIC but not PSCR. These are therefore deducted from NTNIC before arriving at PSCR.

TOTAL MANAGED EXPENDITURE

Public expenditure is measured across the whole of the public sector using the aggregate **Total Managed Expenditure (TME)**. TME is the sum of the public sector current expenditure, public sector net investment and public sector depreciation. These aggregates are based on National Accounts definitions defined under ESA95.

Public sector current expenditure is the sum of expenditure on pay and related costs, plus spending on goods and services, and current grants made to the private sector. Current expenditure is net of receipts from sales of goods and services.

Public sector capital expenditure is shown in Table C15. It includes:

- gross domestic fixed capital formation (i.e. expenditure on fixed assets such as schools and hospitals, roads, computers, plant and machinery and intangible assets) net of receipts from sales of fixed assets (e.g. council houses and surplus land);
- grants in support of capital expenditure in the private sector; and
- the value of the physical increase in stocks (for central government, primarily agricultural commodity stocks).

Public sector net investment: in Table C1 nets off depreciation of the public sector's stock of fixed assets.

Public sector depreciation: is the annual charge that is made in relation to the reduction in value of the public sector's capital assets over a particular financial year.

For budgeting purposes, TME is further split into Departmental Expenditure Limits (DEL) and Annually Managed Expenditure (AME):

Departmental Expenditure Limits (DEL) are firm three-year spending limits for departments. In general DEL will cover all running costs and all programme expenditure except that spending that is included in departmental Annually Managed Expenditure due to it not being reasonably subject to close control over the three year period. DEL has distinct resource and capital budgets, as shown in Table C13.

Annually Managed Expenditure (AME) is spending that cannot be reasonably subject to firm multi-year limits. AME components are shown in Table C11 and are defined as follows.

Social security benefits in AME expenditure covers contributory, non-contributory and income-related benefits for children, people of working age and pensioners. Broadly, benefits are paid in respect of retirement, unemployment, incapacity, or disability, caring responsibilities and bereavement, as well as housing costs for all groups with effect from Budget 2004. Some expenditure on housing-related benefits is, however, covered by the locally financed expenditure category.

Tax credits for individuals scored as expenditure includes that element of the Working Tax Credit and the Child Tax Credit that is classified as public expenditure under national accounts definitions.

Common Agriculture Policy expenditure comprises direct payments to farmers and market price supports (intervention purchases and export refunds). In the national accounts this is treated as a transaction between the EU and the farmers, so it is removed in the accounting adjustments and does not score in TME.

Net public service pensions expenditure is reported on national accounts basis and reflects the difference between the cash paid out during the year and any contributions received for the main unfunded public service pension schemes.

National Lottery expenditures relate to the distribution of the money received from the National Lottery for good causes. Funds are drawn down by Distributor Bodies and directed towards Lottery funded projects.

Non-cash items in AME. Under the current resource budgeting regime, a department's spending budget includes certain items that do not have a cash component at the time when the expense is recorded. Examples include depreciation, cost of capital charges and provisions.

Other departmental expenditure aggregates all other expenditure made by departments that is not separately identified in the AME table.

Net payments to European Union (EU) institutions is the balance between the UK's gross contribution to the EU Budget minus the UK abatement and public sector receipts from the EU Budget (net contribution to EU budget). For domestic public expenditure planning purposes part of the UK's contribution to the EU budget is attributed to the overseas aid programme and excluded from the net payments to EU institutions figures. In the national accounts, Common Agriculture Policy expenditure is treated as a transaction between the EU and farmers, so the associated receipts from the EU are removed in the accounting adjustments and do not score in TME.

Locally financed expenditure consists of local authority self-financed expenditure (LASFE) and Scottish spending financed by local taxation (non-domestic rates and, if and when levied, the Scottish variable rate of income tax), LASFE is the difference between total local authority expenditure, including most gross debt but net of capital receipts, and central government support to local authorities (i.e. Aggregate External Finance (AEF), specific grants and credit approvals).

Central government debt interest is shown gross – only interest paid within the public sector is netted off. All other receipts of interest and dividends are included in current receipts. The capital uplift on index-linked gilts is also scored here as interest at the time it accrues as is the amortisation of discounts on gilts at issue.

Public corporations' own-financed capital expenditure. This is the amount of capital expenditure by public corporations that is not financed by general government.

AME margin is an unallocated margin on total AME spending and is included as a measure of caution against AME expenditure exceeding its forecast levels.

The **accounting adjustments** reconcile the DEL and AME framework of departmental budgets to the national accounts measure of TME, and are shown in Table C14.

Tax credits adds in spending on individuals' tax credits which is scored as negative tax in net taxes and national insurance contributions but as public expenditure in National Accounts. As explained in the public sector current receipts section this mainly includes elements of WFTC and DPTC, which were replaced by new tax credits in 2003-04.

European Community contributions deduct traditional own resources (i.e. payments of customs duties and agricultural and sugar levies) and VAT contributions to the EC, which are included in the net payments to EC institutions line in AME but excluded from TME.

Other central government programmes covers various items which relate to central government programme expenditure and where budgeting and national accounts treatment differ, for example the depreciation costs of NHS trusts and tax credits for companies.

Vat refunds adds back refunds obtained by central government departments, local authorities and certain public corporations. DEL and AME programme expenditure are measured net of these refunds, while TME is recorded with VAT paid.

Central government non-trading capital consumption (i.e. depreciation) as measured by ONS for national accounts is added.

Non-cash items in resource budgets and not in TME includes cost of capital charge, write-offs, notional audit fee, take-up, movements in the value, and release of provisions, the subsidy and bad debt element of student loans, and movement in stocks.

Expenditure financed by revenue receipts adds in certain receipts which are deducted from departmental budgets but which are not treated as negative expenditure in TME.

Local authorities adds in local authority depreciation and subsidies paid to local authority trading bodies, and deducts capital grants from local authorities to public corporations, local authority receipts of investment grants from private sector developers and certain license fees collected by local authorities.

General government consolidation adjusts for the fact that payments of certain taxes, grants and interest that are within the public sector do not score in TME, as TME is a consolidated public sector concept.

Public corporations adds receipts from public corporations of interest, dividends and equity withdrawals that are netted-off in budgets, interest paid by public corporations to the private sector and abroad (as property income paid by the public sector to the rest of the economy is in TME, but not in departmental budgets) and deducts the profit/loss of the Forestry enterprise.

Financial transactions deducts net lending, acquisition of securities and profit/loss on sale of financial assets.

Other accounting adjustments deducts depreciation and impairments in AME, removes expenditure on the CAP and the associated receipts from the EU and reconciles to national accounts outturn.

