Autumn Statement 1983

HM TREASURY
NOVEMBER, 1983

Autumn Statement 1983

RETURN to an Order of the House of Commons dated 17 November 1983: for

COPY of the AUTUMN STATEMENT 1983 as laid before the House by the CHANCELLOR OF THE EXCHEQUER on 17 November 1983

Treasury Chambers, 17 November 1983 } NIGEL LAWSON

Ordered by The House of Commons *to be printed*
17 November 1983

LONDON
HER MAJESTY'S STATIONERY OFFICE
£4·00 net

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1. Economic Prospects for 1984

Summary

World economy

1.01 A vigorous rise in activity in the US is not being matched elsewhere: in parts of Europe, in OPEC, and in many of the developing countries, activity and imports have fallen, in the process of adjustment to international or national debt problems. World trade is only now beginning to recover after the fall of the last two years.

Output, demand and employment

1.02 In the UK, however, output has been rising since 1981, as real domestic demand has recovered, helped by falls in inflation and interest rates. Output in 1983 is expected to be about 3 per cent higher than in 1982. The growth in domestic demand is likely to slow down perhaps from 4 per cent in 1983 to 3 per cent in 1984, but a continued rise in investment and a recovery in exports should sustain the growth in activity. With world demand recovering, and the profitability of home supply increasing, the forecast is for UK output to grow by 3 per cent in 1984 and for employment to rise.

Balance of payments

1.03 The main factor in the sharper growth of imports relative to exports since 1981 has been the recovery in domestic demand in the UK, ahead of most other industrial countries. This has been reflected in the current account of the balance of payments, where a surplus of over £5 billion in 1982 has given way to a small surplus in the first nine months of 1983. With a recovery forecast for exports, the current account may remain near balance in 1984. The forecast assumes that the exchange rate will not change much from recent levels.

Inflation

1.04 This year has again seen a lower than expected rate of inflation in the UK. Costs are rising more slowly than prices, leaving room for a sizeable recovery in profitability from an historically low base. At the same time the real income of those in work has risen. Current inflationary pressures continue weak and by the end of next year inflation should be below the current rate of about 5 per cent.

Borrowing

1.05 The PSBR in this financial year, 1983–84, looks like turning out higher than expected at Budget time. This is despite the July 7 measures and partly reflects the same factors that caused higher than expected spending at the end of 1982–83. For 1984–85, this forecast continues to assume, as in the Medium Term Financial Strategy, a PSBR of $2\frac{1}{2}$ per cent of GDP, or £8 billion. The present forecast, subject to a wide margin of error, assumes an increase of taxation in order to achieve this, after allowance for indexation of personal taxes and specific duties.

Monetary policy

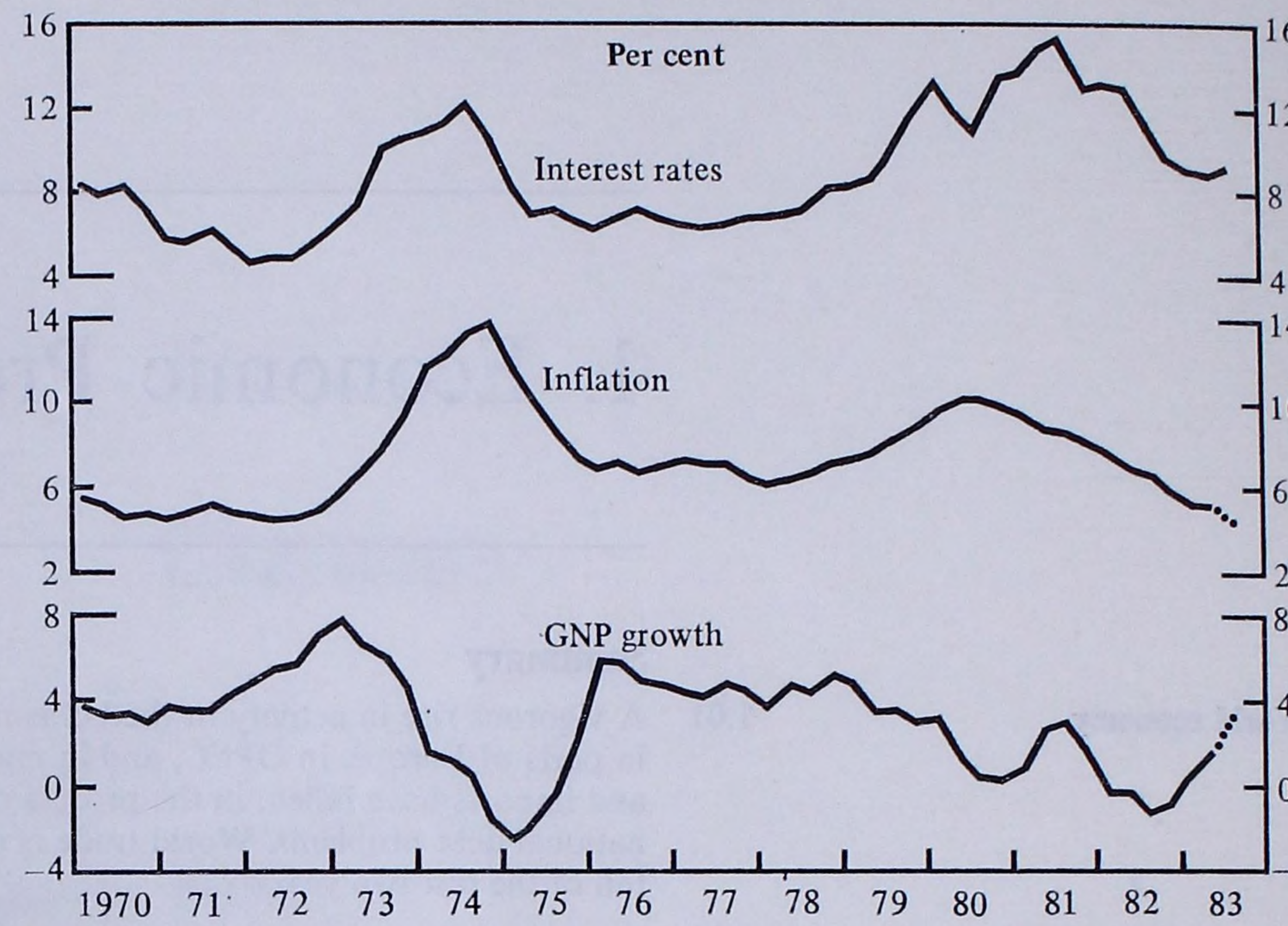
1.06 Monetary policy in 1984–85 is assumed, like fiscal policy, to be consistent with the indications given in the MTFS. These included a range for monetary growth of 6–10 per cent.

The world economy

Recent developments

1.07 Output rose in all the major countries in the first half of 1983. Rapid growth in the US continued into the third quarter, but the recovery in Europe has been weak and erratic. Underlying inflation in the major six economies has fallen to about 5 per cent. Interest rates in most countries remain high in real terms. The upward trend in unemployment has slowed substantially in many countries, and is being reversed in the US.

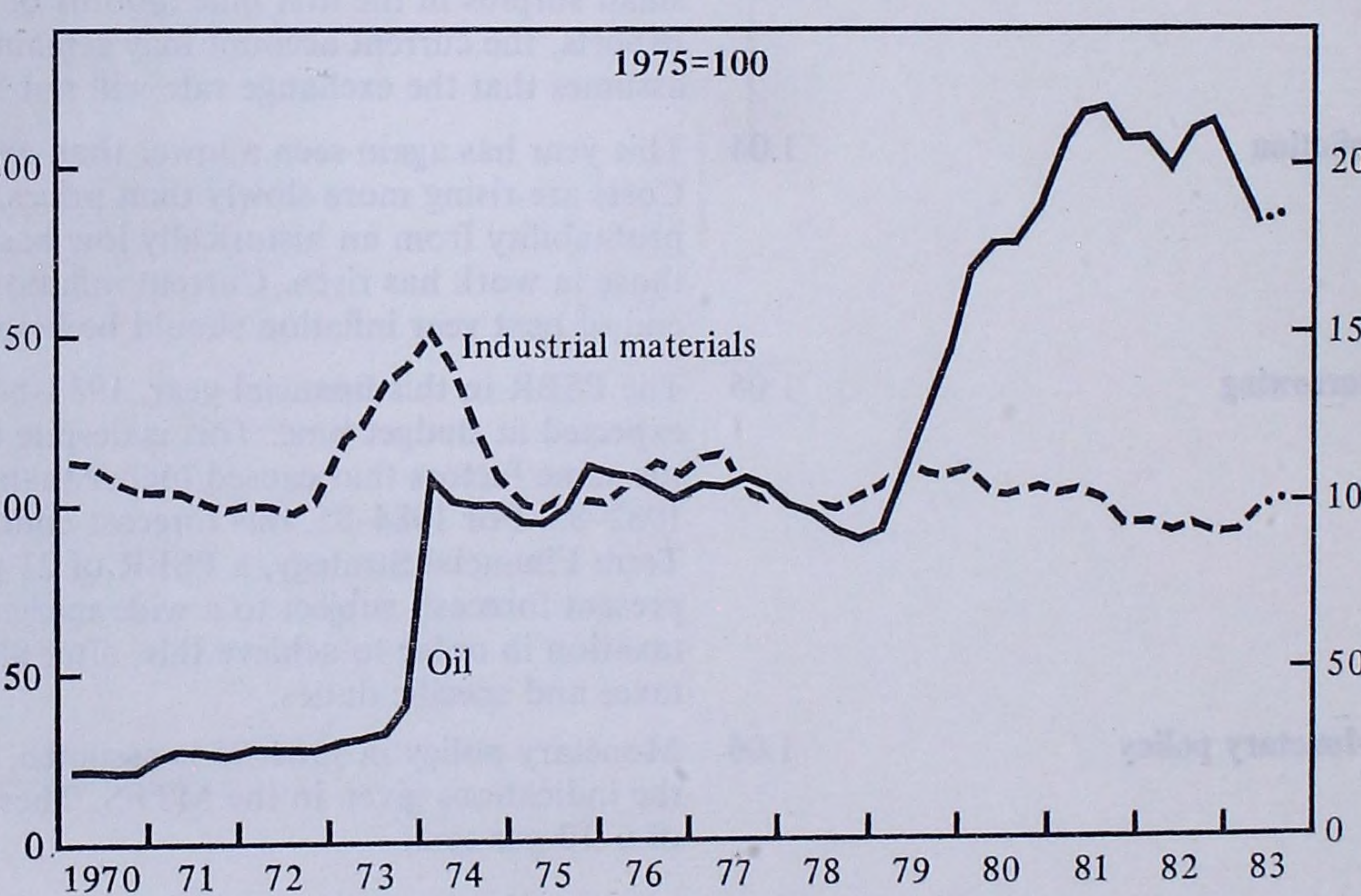
CHART 1.1 **Overseas economies (major six countries)***



* US, Japan, Germany, France, Italy and Canada.

1.08 After falling substantially during 1982 world trade in manufactures appears to be growing again in the course of this year, largely as a result of the growth of imports into the US. Many developing countries, including some members of OPEC, have had to reduce imports sharply because of falls in their earnings from primary products and because of difficulties in meeting debt obligations or obtaining fresh bank credit. Oil prices fell earlier this year in the face of a substantial fall in demand but other commodity prices have been rising from very low levels in 1982.

CHART 1.2 **Commodity prices***



* In relation to prices of manufactured exports

Prospects

1.09 Recovery in the US is expected to moderate after the rapid growth in mid 1983. In Europe recovery should resume in 1984 after some faltering in the second half of this year. Inflation, overall, may not change much, with a slight rise in the US matched by further falls in Europe. Outside the OECD area, the timing and extent of recovery in imports, as the need lessens for further downward adjustment, is very uncertain. On the assumption of improved export earnings and financial flows, developing countries should be able to sustain renewed growth in imports in 1984. The recovery in world trade should be faster than that in output: this is the normal pattern in an upswing of the cycle, but seems not to have occurred in 1983 because of sizeable falls in imports in many countries outside the major six.

1.10 The outlook for the world economy is summarised in the table below.

Table 1.1 World economy

Percentage changes on a year earlier

	Average 1975–82	1981	1982	1983	1984
GNP*	3	2	−½	2½	3½
Prices* (consumers' expenditure deflator)	8½	9	7	5	5
World trade in manufactures (weighted by UK markets)	4	3½	−3	−1	5

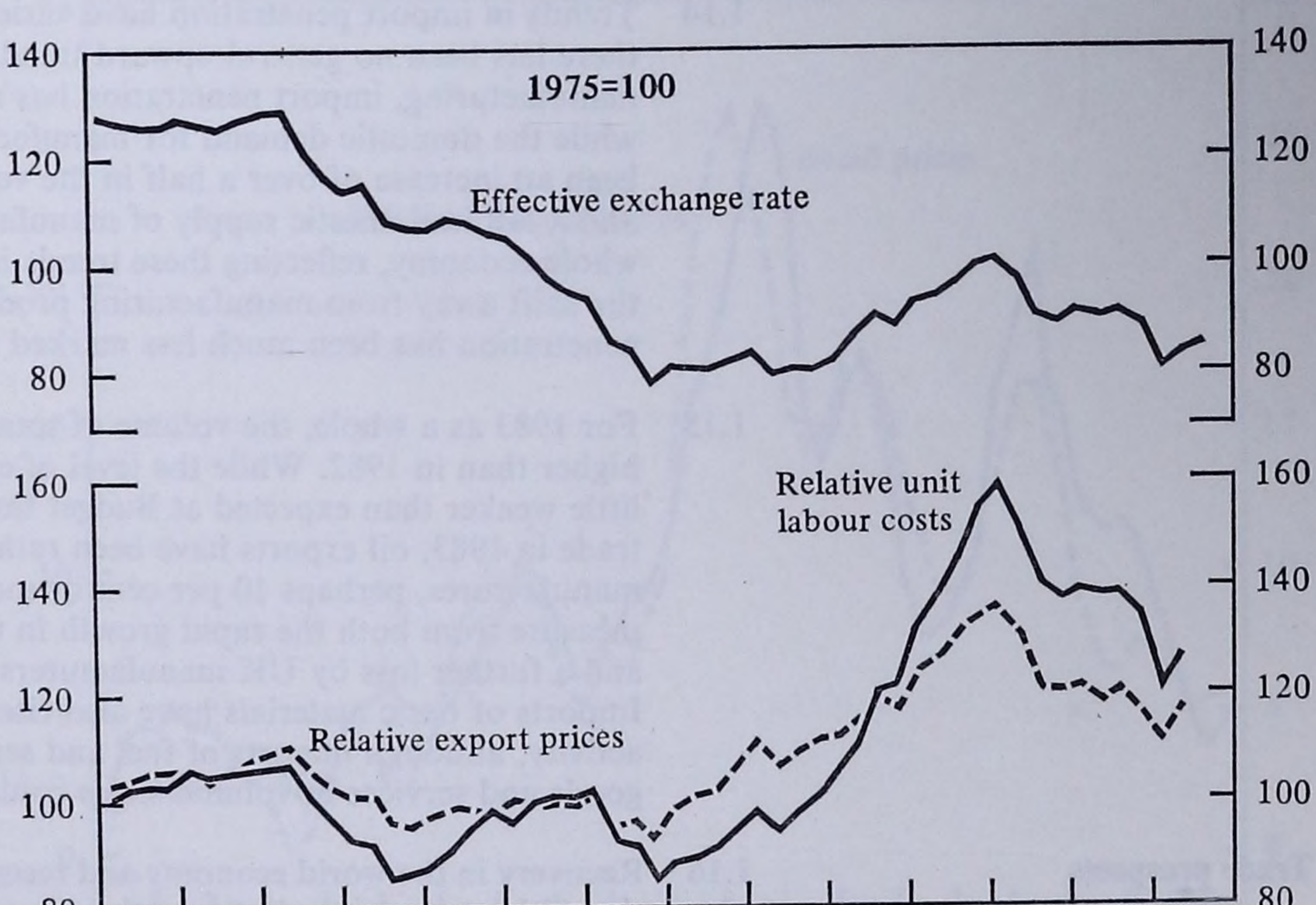
* Major six countries (US, Japan, Germany, France, Italy, Canada)

The exchange rate, relative costs and trade

Relative costs

1.11 Over the course of the last two and a half years there has been a partial reversal of the sharp deterioration in relative costs in the 1978–81 period. Between the first halves of 1981 and 1983 the level of domestic unit labour costs in manufacturing relative to those of our competitors is estimated to have fallen 20 per cent. This was rather more than the fall in the effective exchange rate: above average productivity gains, and reductions in the National Insurance Surcharge, partly offset by slightly higher earnings growth in the UK, resulted in domestic costs in manufacturing rising slightly less than those of our competitors. For the purposes of this forecast it is assumed that the effective exchange rate will not change much from the average level for the first three quarters of 1983. Further gains in relative costs are likely to depend on improvements in UK unit labour costs relative to those overseas.

CHART 1.3 **The exchange rate; and relative prices and costs in manufacturing industry**

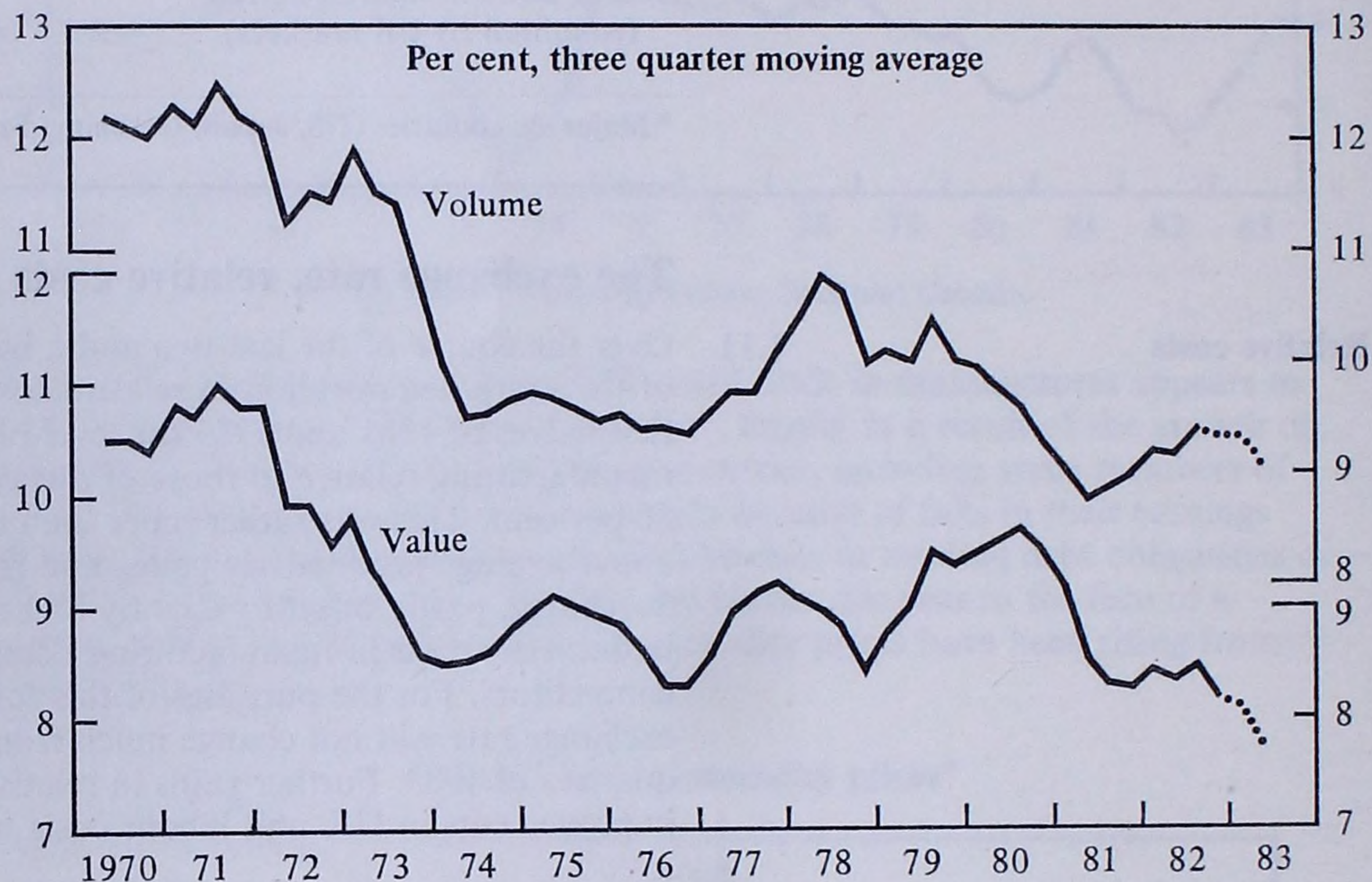


Trends in trade

1.12 Over the course of the 1970s and early 1980s a number of structural changes have been taking place in the UK economy. These have been reflected in the diverse movements of the components of the visible trade balance. The surplus on non-manufactured goods has been on a rising trend, and the balance of trade in oil has moved from a deficit of 3 per cent of nominal GDP in 1976 to a surplus of $1\frac{1}{2}$ per cent last year. But the balance of trade in manufactures, as a percentage of nominal GDP, has shown a falling trend over this period.

1.13 Over the past 10 years there has been no pronounced trend in value or volume terms in the share of UK's manufactured exports in world trade, despite substantial short-term fluctuations. (Chart 1.4). Since 1981 the volume share has tended to rise while the value share, reflecting lower relative prices, has fallen.

CHART 1.4 **Shares of UK exports in world trade in manufacturing**



1.14 Trends in import penetration have varied by sector. Outside manufacturing there has been no general upward trend, with falls in some sectors. Within manufacturing, import penetration has risen strongly. For example since 1976, while the domestic demand for manufactures has not changed greatly, there has been an increase of over a half in the volume of imports of manufactures and a fall in domestic supply of manufactures of nearly one quarter. For the whole economy, reflecting these trends in import propensities and in particular the shift away from manufacturing production, the rising trend in import penetration has been much less marked than for the manufacturing sector.

1.15 For 1983 as a whole, the volume of total exports is expected to be slightly higher than in 1982. While the level of exports of manufactures has been a little weaker than expected at Budget time, reflecting the lower level of world trade in 1983, oil exports have been rather higher. The rise in imports of manufactures, perhaps 10 per cent or more in 1983, results in roughly equal measure from both the rapid growth in the domestic demand for manufactures and a further loss by UK manufacturers of share in the domestic market. Imports of basic materials have also risen this year with the recovery in domestic activity, although imports of fuel and services have tended to fall. Imports of goods and services in volume terms could be 5 per cent higher than in 1982.

Trade prospects

1.16 Recovery in the world economy and recent improvements in UK competitiveness should lead to a period of growth in export volumes. This would be consistent with recent evidence from the CBI survey, where there is a positive balance of respondents optimistic about export prospects. With North Sea oil production approaching its peak, exports of fuels are expected to be broadly unchanged from recent levels. Exports of manufactures, non-manufactured goods and services are all projected to increase. Further growth in import volumes of manufactures is likely in 1984, as the economy continues to expand, although import volumes for non-manufactures, including fuel, may change little from current levels.

Terms of trade

1.17 So far there has been only a small deterioration in the non-oil terms of trade since the peak in early 1981. Some slight further fall is expected, as importers (who no longer seem to be charging higher prices, on average, for manufactures in the UK than elsewhere) raise prices to cover higher costs, including higher commodity prices. Exporters' profit margins should continue to recover.

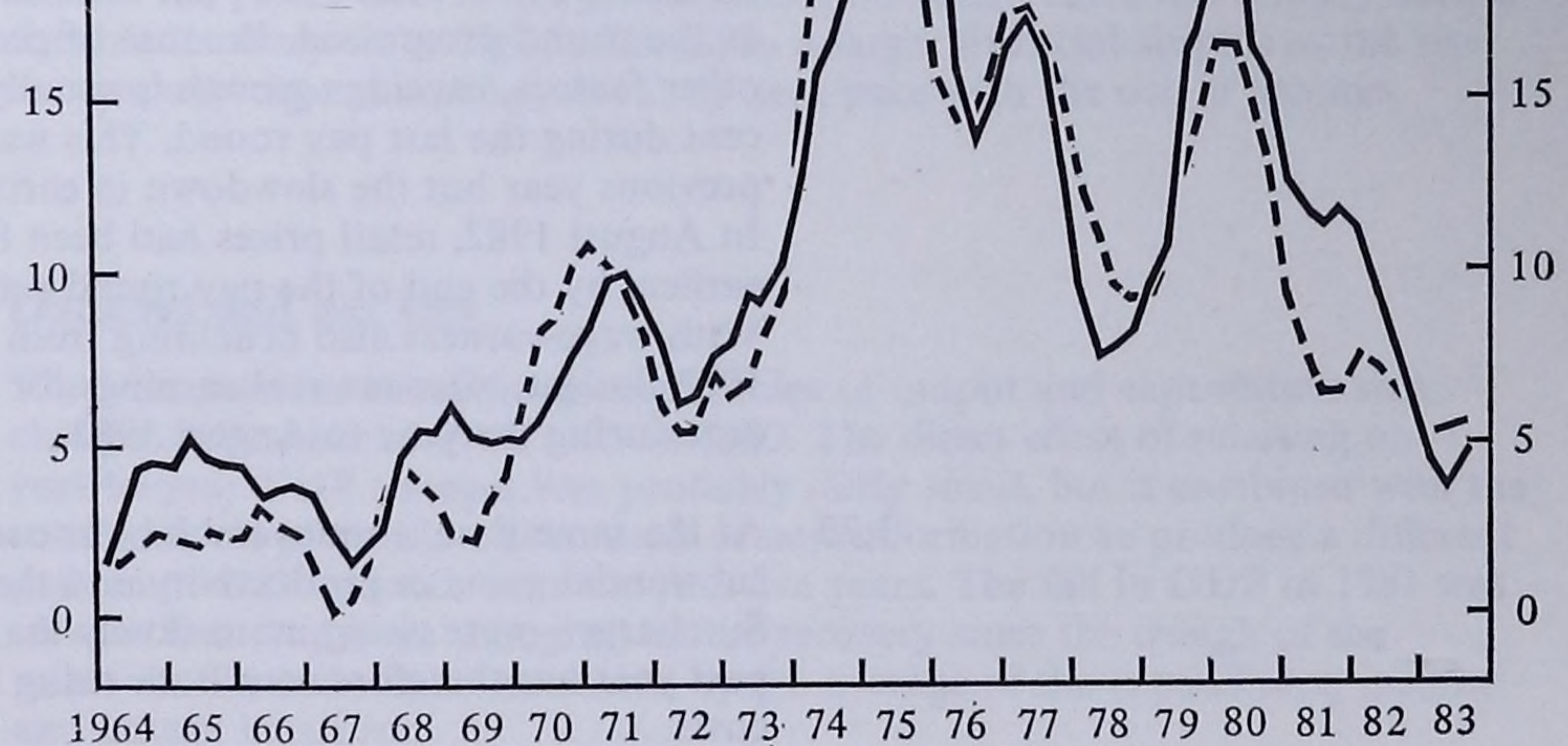
Current balance

1.18 Between 1981 and the first nine months of 1983, the current account of the balance of payments moved from a surplus of £6½ billion to a position of small surplus. Much of this change reflected the earlier recovery in UK demand compared with the rest of the world. But the recovery of world trade now expected for 1984 should lead to growth in exports much more in line with growth in imports. With an increase in the invisibles balance, on services and interest, profits and dividends, the prospect is for broad balance in the current account over the forecast period.

Inflation

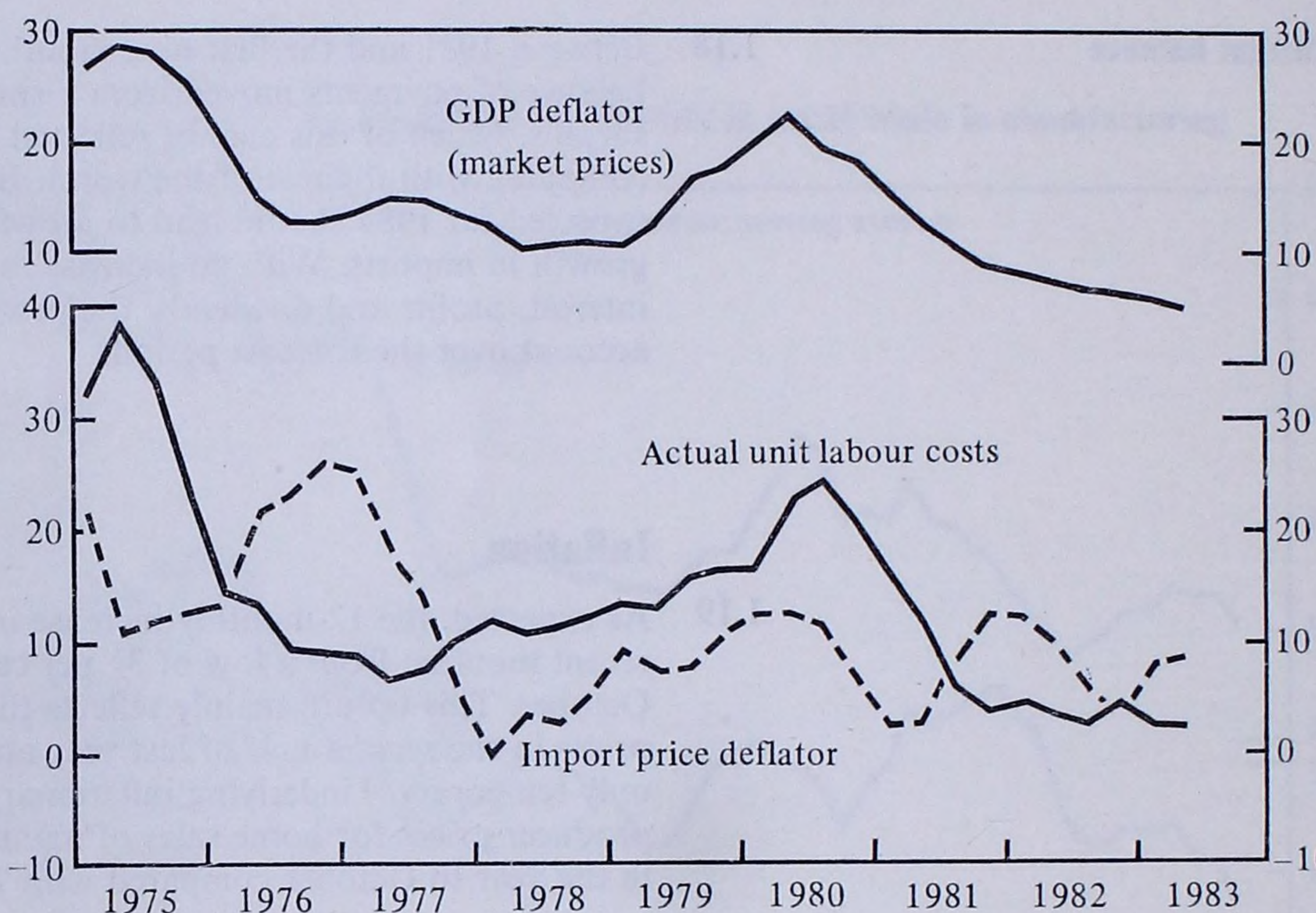
1.19 As expected, the 12-monthly increase in the Retail Prices Index has turned up in recent months: from a low of 3¾ per cent in May and June to 5 per cent in October. This upturn mainly reflects the particularly favourable profile of retail prices in the second half of last year and early 1983 and it is expected to be only temporary. Underlying inflationary pressures remain downward with producer prices for home sales of manufacturing output increasing by 5½ per cent in the year to October compared with 7 per cent a year ago.

CHART 1.5 **Prices: percentage changes on a year earlier**



1.20 The market price GDP deflator rose by 5 per cent in the year to the second quarter of 1983 ($6\frac{1}{2}$ per cent in the financial year 1982–83) compared with 15 per cent at the beginning of 1981. This reflected much smaller rates of increase in the main elements of domestic costs as financial and competitive pressures on industry encouraged lower pay settlements and historically exceptional gains in manufacturing productivity. In the first half of 1983, unit labour costs in the whole economy were only 2 per cent higher than a year earlier, with the reductions in the National Insurance Surcharge helping to limit the growth in industrial costs. Profit margins, squeezed severely in many sectors during the downturn, have been recovering since 1981.

CHART 1.6 **Domestic prices, import prices and labour costs: percentage changes on a year earlier**



Costs

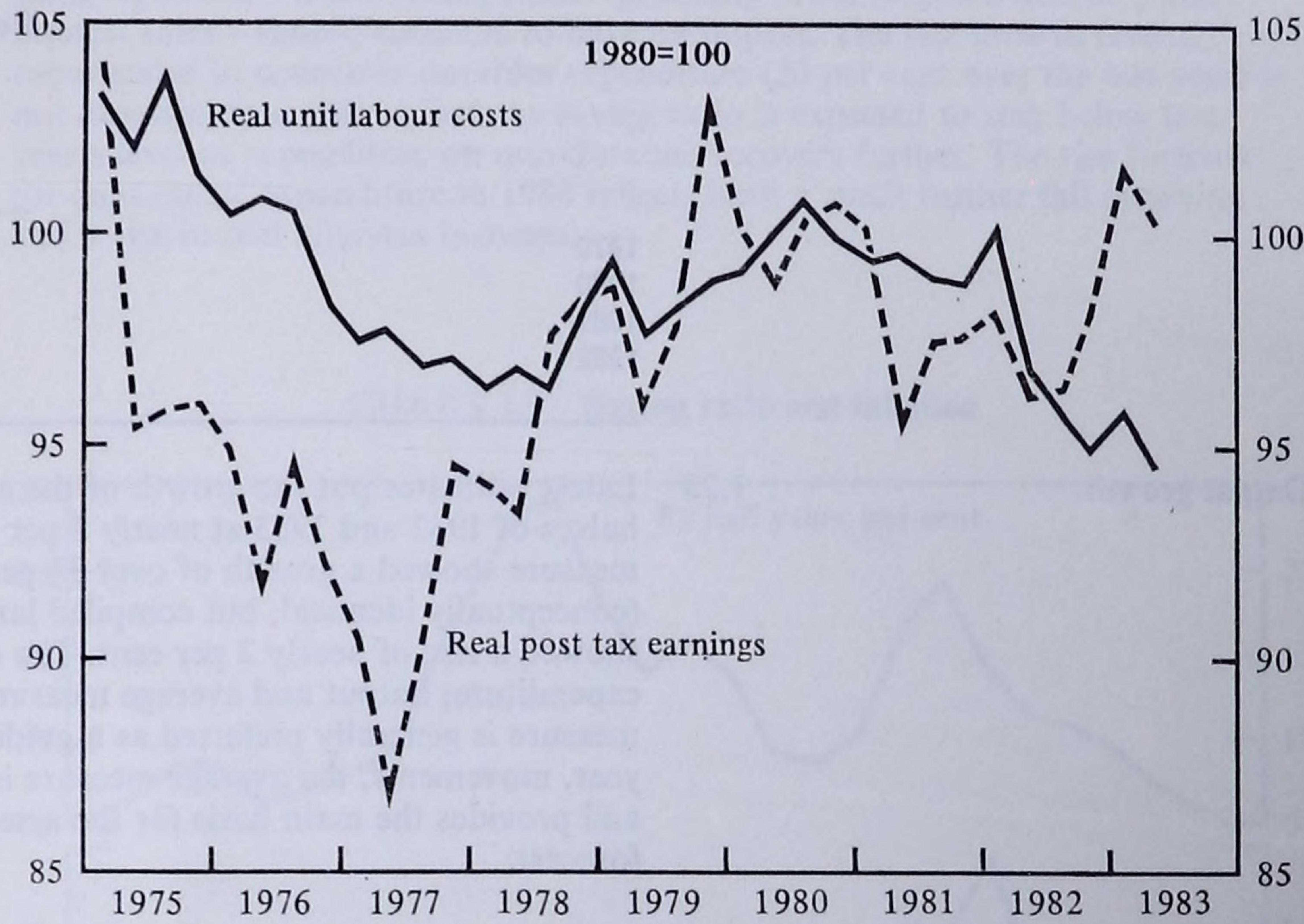
1.21 World inflation rates have also declined appreciably over the last two years, with commodity prices falling through most of 1982. Although some commodities have recovered strongly this year, the effect on the UK economy has been fairly muted. While the spot market rates which enter into some of the most widely-quoted indices of commodity prices have risen rapidly, there has been less impact on the prices at which most trading has actually taken place. Oil prices have also been fairly steady since the fall early in 1983. Import prices, though rising faster than domestic costs, have not provided strong upward pressure on prices charged by domestic producers.

Pay

1.22 Pay settlements in the year ending in August were fairly tightly bunched around an average level of about $5\frac{1}{2}$ per cent. Little variation was observable in settlements as the round progressed. Because of productivity bargaining, grading drift and other factors, earnings growth is usually above settlements and was about $7\frac{1}{2}$ per cent during the last pay round. This was about $1\frac{1}{2}$ per cent less than in the previous year but the slowdown in earnings growth did not match that of prices. In August 1982, retail prices had been 8 per cent above the level of a year earlier; by the end of the pay round retail prices were rising at only 4–5 per cent. With wage-earners also benefiting from the increases in tax allowances in the 1983 Budget, after-tax real earnings for an average employee rose about 4 per cent during the year to August 1983.

1.23 At the same time, employers' labour costs per unit of output—held down by substantial gains in productivity and the reductions in National Insurance Surcharge—were rising more slowly than prices being charged by producers. The past year has therefore seen both rising real earnings and falling real unit labour costs.

CHART 1.7 **Real labour costs and real earnings: whole economy levels**



Prospects

1.24 The current pay round is starting against an improved background for both employees and employers with real take home pay higher and unit labour costs rising more slowly than prices. Competitive pressures are still strong, both on employers in world and domestic markets and on employees in a weak labour market. So, despite the continued recovery in domestic output and a rise in employment over the next year, there should not be a reversal of the downward trend of earnings growth.

1.25 Lower rates of inflation now being achieved in other industrial countries are reinforcing the pressures on domestic industry to keep down prices and costs. Over the next year, allowing for some further recovery in margins, the market-price GDP deflator is expected to rise by about 5 per cent. Taking account of movements in import prices and the recent bumpy path, annual changes in the retail prices index may be a little more volatile. Some further increase—perhaps to about 5½ per cent—is expected for the 12-monthly rate in the first half of next year as past favourable factors drop out of the comparison. These effects should however be short-lived and the 12-monthly increase is expected to fall back, perhaps to around 4½ per cent by the end of 1984.

1.26 Domestic recovery and a rise in external demand, with prices tending to rise faster than costs in most markets, will all contribute to a continuing rise in profits. While profitability for most industrial and commercial companies, outside the North Sea, is not yet back to 1979 levels, there has already been a sizeable recovery since 1981, reflected in a larger financial surplus as the rise in company expenditure has not fully kept pace with the rise in income.

Demand and activity

1.27 The base year for constant-price estimates of output and expenditure was changed this summer from 1975 to 1980. The direct effect of rebasing on year-to-year GDP changes was probably fairly small, but it combined with the usual process of revision as a result of new information to produce a different pattern of GDP growth over the past five years. The fall in GDP in 1981 was smaller than had been thought and the recovery since the trough of the recession has been faster as shown by the average of the expenditure, income and output measures.

Table 1.2 Measures of GDP (Average)

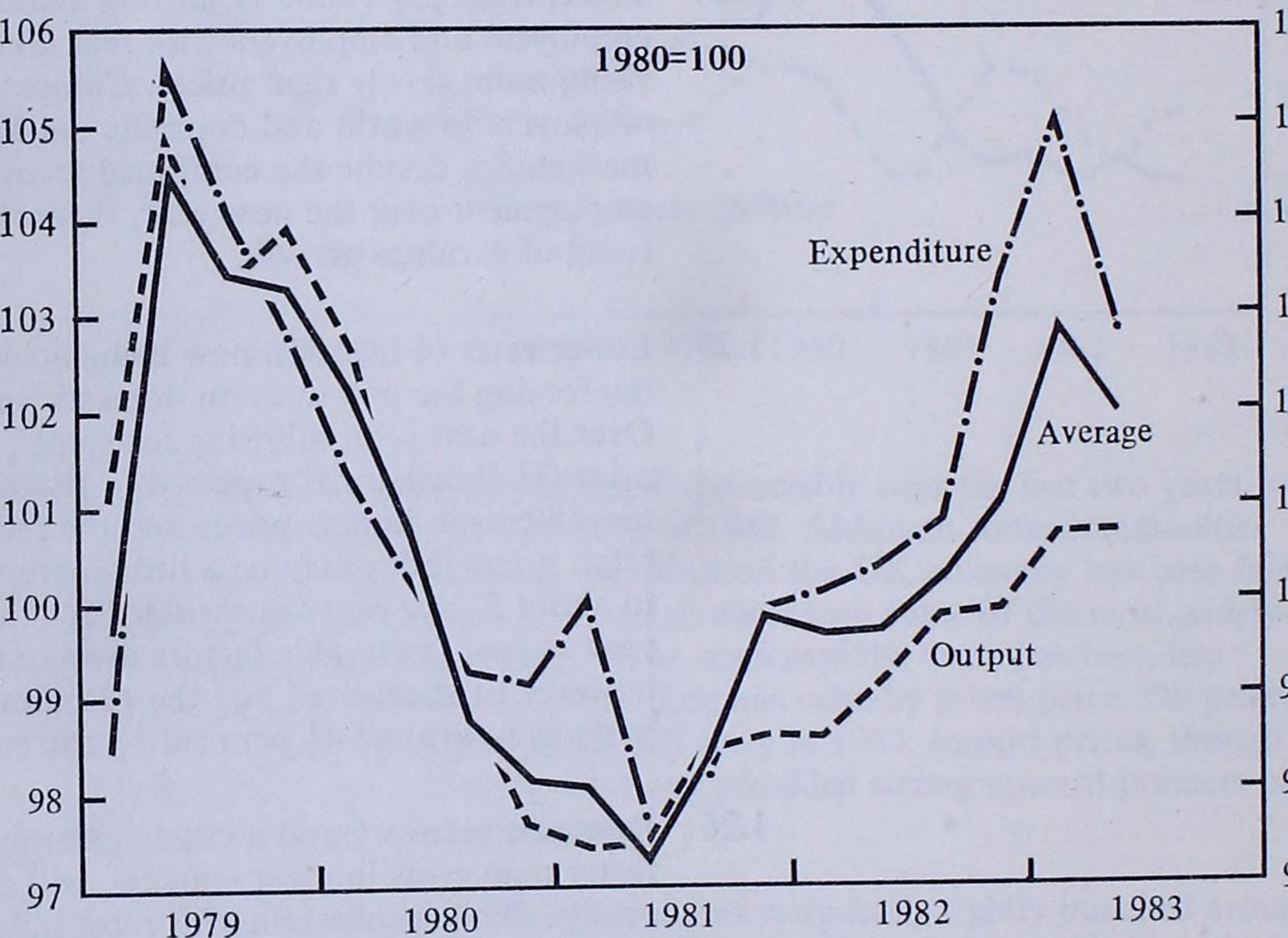
Percentage changes on a year earlier

	Estimates made in spring 1983 (1975 prices)	Latest estimates (1980 prices)
1979	+2	+2½
1980	−2½	−2½
1981	−2½	−1½
1982	+1	+2

Output growth

1.28 Latest estimates put the growth of the average measure of GDP between the first halves of 1982 and 1983 at nearly 3 per cent. Within this average the expenditure measure showed a growth of over 3½ per cent while the output measure (conceptually identical, but compiled largely from independent data sources) showed a rise of nearly 2 per cent. The chart below shows the movements in the expenditure, output and average measures of GDP. Although the output measure is generally preferred as a guide to shorter-term, particularly within year, movements, the average measure is usually more reliable for longer periods and provides the main basis for the assessment of activity movements in this forecast.

CHART 1.8 **Measures of GDP**



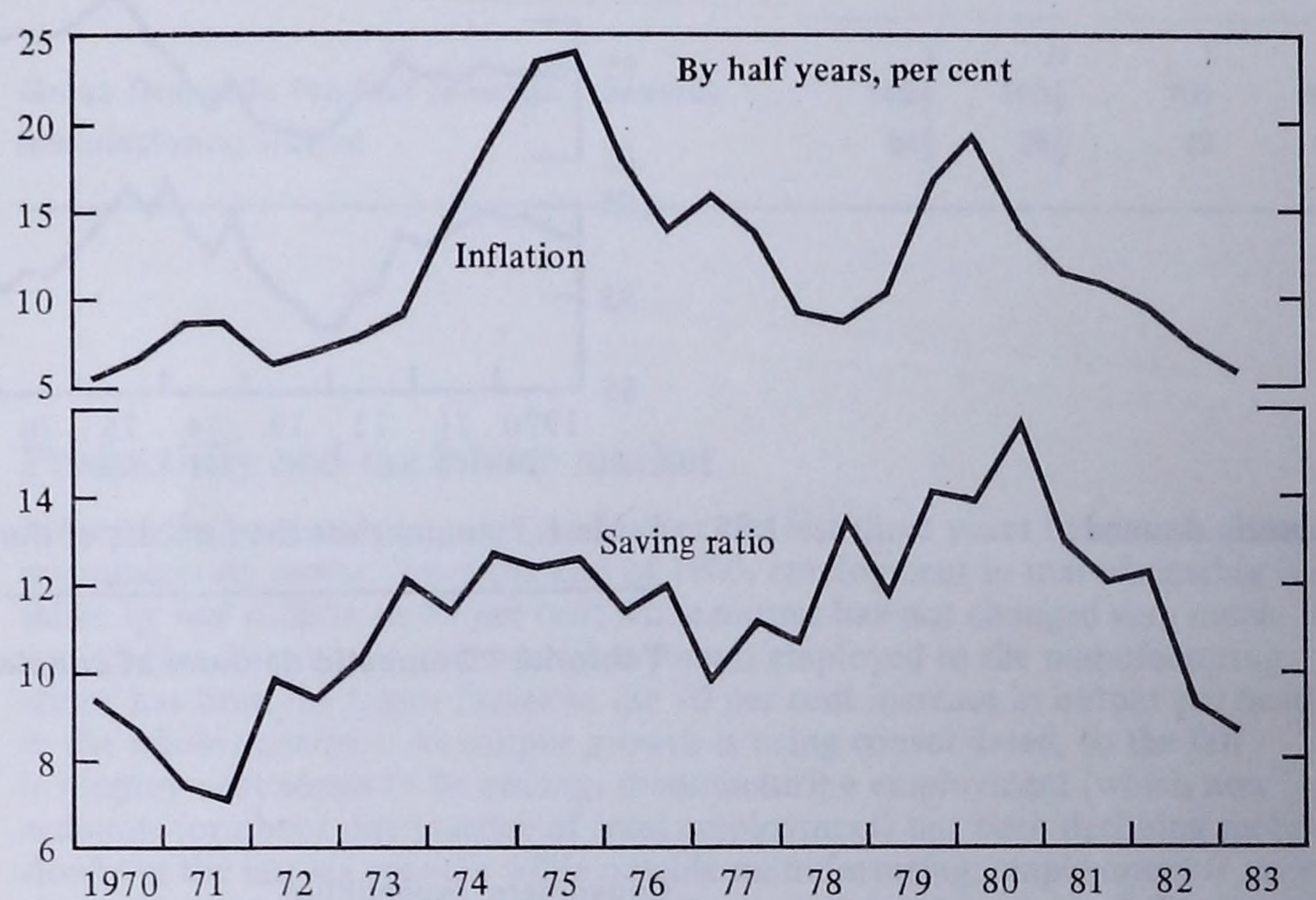
1.29 The buoyancy of GDP over the past year has reflected recovery in domestic demand. Consumers' expenditure, which had been virtually flat over the previous three years, rose by 3 per cent in the second half of 1982 and a further 1½ per cent in the first half of 1983. Fixed investment, particularly in dwellings, is recovering.

Personal consumption

1.30 Since the first half of 1982 real personal disposable income, in total, has been little changed. The rise in consumers' expenditure (and the fall in the saving ratio from over 12 per cent in the first half of 1982 to over 8½ per cent in the first half of 1983) has been mainly financed by a rise in borrowing. Lower inflation and lower interest rates have been major factors in the fall in saving: lower inflation has meant that consumers have needed to save less to maintain the real value of their financial wealth. In the 1960s, when inflation averaged 4 per cent the saving ratio averaged 8 per cent.

1.31 Total real personal disposable income is now beginning to rise again as real take home pay rises and employment stops falling. But other factors bringing about a lower saving ratio—primarily lower inflation and nominal interest rates—should continue to have an impact. The fast growth recently experienced in consumer durables expenditure (20 per cent over the last year) is not expected to continue, but the saving ratio is expected to stay below last year's level as expenditure on non-durables recovers further. The rise forecast for consumers' expenditure in 1984 reflects both a small further fall in saving and a rise in real after-tax incomes.

CHART 1.9 **Saving ratio and inflation**



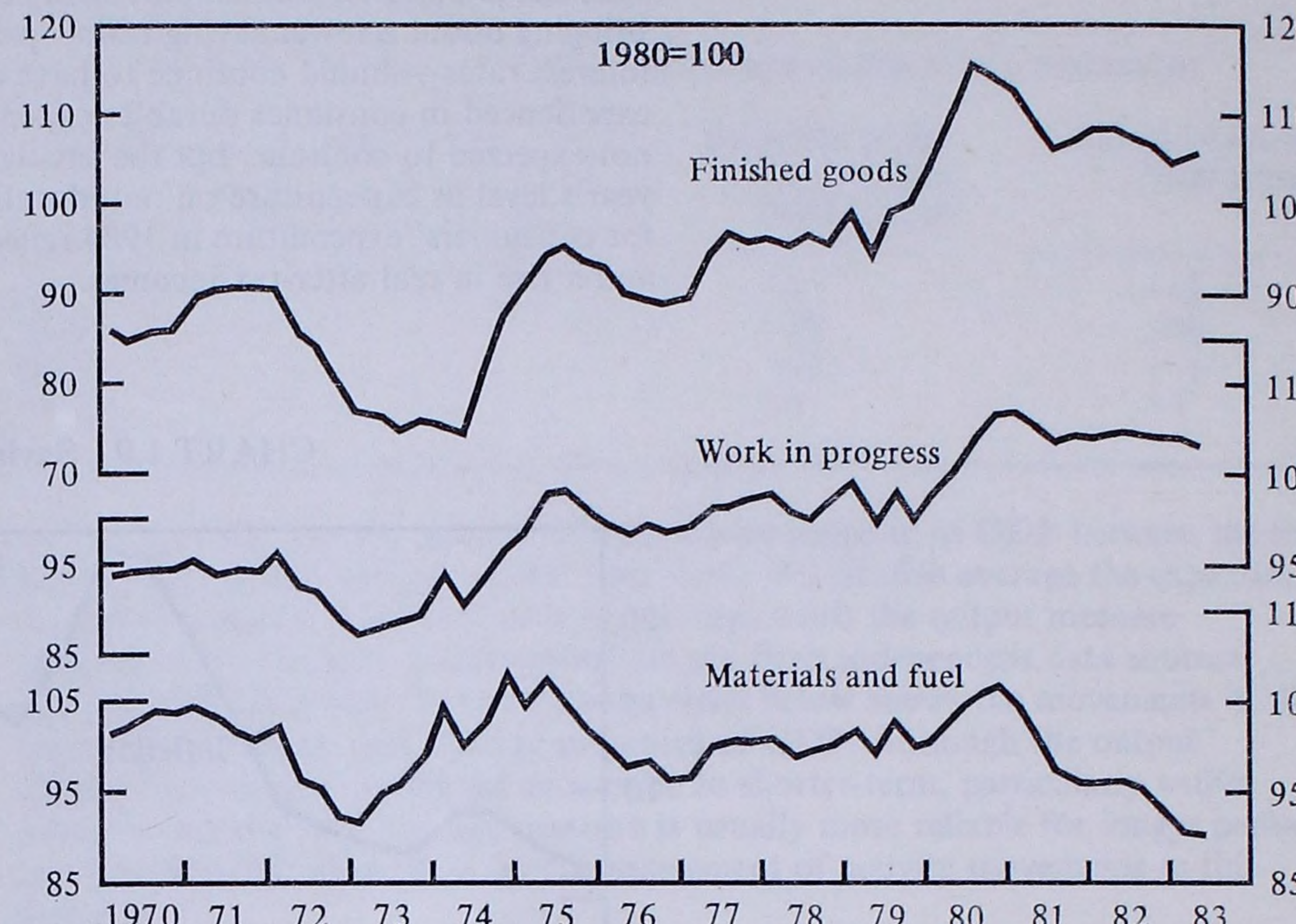
Investment

1.32 Total fixed investment, which fell in 1980 and 1981, rose in 1982, and in the first half of 1983 was nearly 3 per cent up (at constant prices) on a year earlier. Two areas of private fixed investment—housebuilding and investment by manufacturing industry—fell sharply in the recession. Manufacturing investment, which normally lags the economic cycle, has fallen by over a third since the 1979 peak but is now showing signs of levelling out. Private investment in dwellings had risen about 15 per cent above its 1981 average by the first half of 1983. Outside manufacturing, business investment has been much less affected. Only small falls were recorded in 1980 and 1981 and investment in this area now seems to be growing at an annual rate of some 6 per cent.

1.33 Surveys point to a steady growth in industrial investment, including manufacturing investment, in 1984 reflecting recent and prospective rises in output and profits. Taking account of continued buoyancy in private housing and some recovery in public investment as output and trading prospects for the nationalised industries continue to improve, total fixed investment is forecast to rise by 4 per cent in 1984.

1.34 The improvement in prospects for industrial investment reflects in part the better financial position of the company sector as margins as well as output recover. This is also expected to relieve some of the pressure on stock levels. Much of the destocking in 1980 and 1981 reflected companies' need to improve their cash flow at a time of high interest rates and poor output expectations. 1982 saw some fluctuations in stocks: a rebuild in the first half year being reversed in the second half as industrial confidence faltered briefly and then final, domestic demand proved stronger than expected. Recent surveys suggest that, with expectations of output growth fairly stable, stock-output ratios may not depart radically from current levels.

CHART 1.10 **Manufacturers' stock-output ratios**



Domestic demand

1.35 Table 1.3 summarises the forecast of domestic demand.

Table 1.3 Domestic demand at constant prices

Percentage increases on a year earlier

	1982	1983	1984
Consumers' expenditure	1½	3½	2½
Change in stockbuilding (as per cent of GDP level)	1	1	½
Fixed investment	6	2½	4
Public consumption	1½	2½	1
Total Domestic Demand	**3**	**4**	**3**

Demand and activity

1.36 As the UK and world recoveries become more firmly established the composition of final expenditure is expected to begin to shift away from personal consumption towards exports and industrial investment. The improvement in the relative cost position of domestic industry over the last two years should also limit the proportion of additional demand met by imports, though, overall, the rising trend in import propensities is forecast to continue. But the growth in imports should be more nearly matched by the growth in exports.

Table 1.4 Expenditure and GDP

Percentage increases on a year earlier

	1982	1983	1984
Domestic demand*	3	4	3
Exports of goods and services*	1½	½	4
Imports of goods and services*	3	5	5
Domestic Production—GDP at factor cost (Average measure)	2	3	3

* Expenditure measures at market prices.

1.37 Manufacturing output resumed its slow recovery at the beginning of 1983 and latest data suggest that the level of output in mid-year was about 3 per cent above the trough of the first quarter of 1981. In the same period, the average measure of GDP rose by about 5 per cent. With the expected recovery in exports and fixed investment, the growth in manufacturing production in 1984 may not be very different from that of the economy as a whole.

Table 1.5 Output

1980 = 100

	1983		1984	
	I	II	I	II
Gross Domestic Product (average measure)	$102\frac{1}{2}$	$103\frac{1}{2}$	105	$106\frac{1}{2}$
Manufacturing Output	$94\frac{1}{2}$	$95\frac{1}{2}$	97	98

Productivity and the labour market

Productivity and the labour market 1.38 Most of the productivity gains made over the last three years have been in the manufacturing sector. Since the end of 1980, employment in manufacturing has fallen by one million or 15 per cent while output has not changed very much. The rise of over 18 per cent in output per person employed in the manufacturing sector has been the major factor in the 10 per cent increase in output per head in the whole economy. As output growth is being consolidated, so the fall in employment seems to be ending; manufacturing employment (which now accounts for about one quarter of total employment) has been declining more slowly in the last six months while outside manufacturing, employment is now rising. Unemployment may now be levelling off. Other labour market indicators, notably unfilled vacancies and hours worked, are pointing to some recovery in the pressure of demand for labour.

1.39 Recent statistics for productivity are shown in table 1.6.

Table 1.6 Productivity

Indices, 1980 = 100

	Whole Economy			Manufacturing		
	Employment million	GDP average measure	GDP per person employed	Employment million	Output average measure	Output per person employed
1980 H1	25·3	101·5	100·7	7·2	104·7	102·0
H2	24·9	98·5	99·3	6·8	95·3	98·0
1981 H1	24·3	97·7	100·6	6·4	92·1	100·2
H2	24·0	99·1	103·5	6·2	94·6	106·5
1982 H1	23·8	99·7	104·9	6·0	94·2	108·9
H2	23·6	100·6	106·8	5·9	93·3	110·7
1983 H1	23·5	102·4	109·1	5·7	94·4	115·0

1.40 The cost pressures on manufacturing in the 1980–81 period were greater than in other sectors of the economy; and international comparisons suggest that the scope for productivity gains in manufacturing was substantial. The rapid productivity gains of the last three years, going well beyond the usual cyclical recovery, reflect improvements in use of existing plant as well as, in some cases, closure of less efficient units, and changes in the composition of the manufacturing sector.

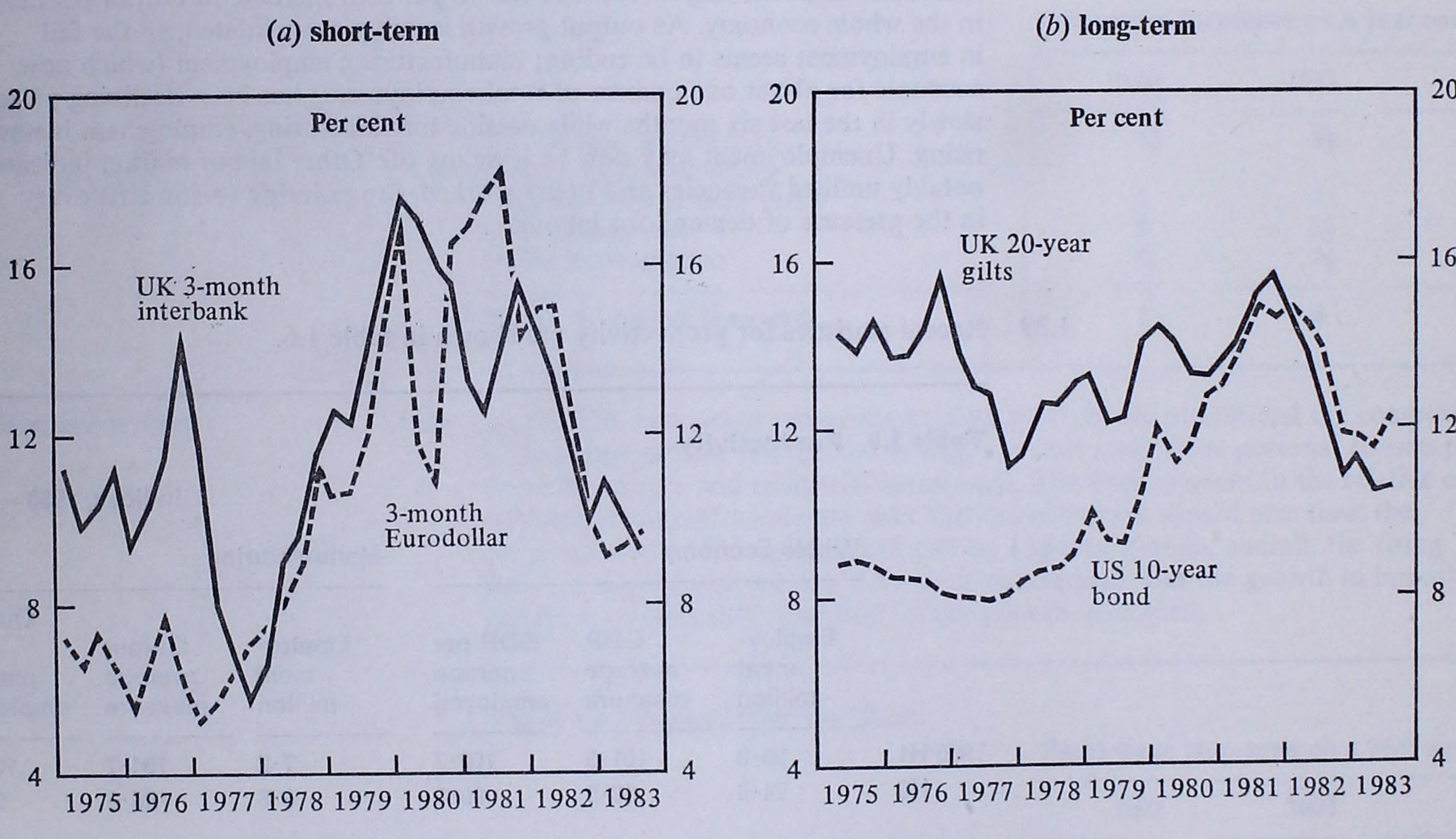
1.41 The forecast incorporates the view that the gains of recent years will be consolidated into higher productivity levels; but that, apart from the normal effect of the continuing cyclical recovery, the underlying growth of productivity will be slower than in the last three years but faster than the 1 per cent a year growth recorded for manufacturing between 1973 and 1979. Outside manufacturing the somewhat uncertain data do not suggest above average gains in recent years. Overall the forecast is consistent with a rise in employment over the next year.

Monetary growth and fiscal projections

Money supply and interest rates

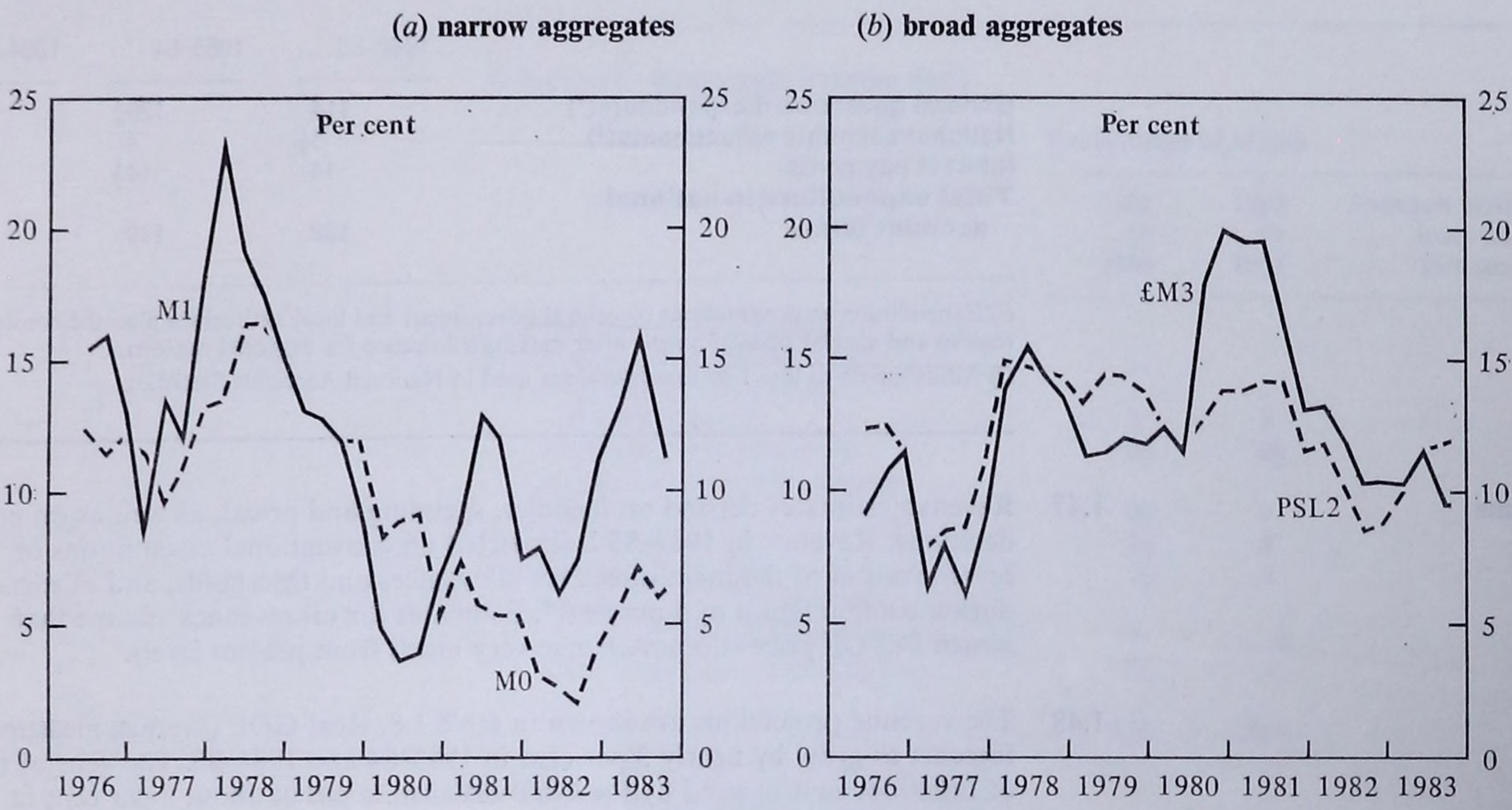
1.42 US interest rates which had fallen rapidly during 1982 rose a little in 1983, in response to the rapid recovery in activity and to the faster rise in monetary aggregates. In the other major OECD economies, there were no significant changes in interest rates. The relationship between the UK and Eurodollar short-term rates is shown in the first part of chart 1.11 and the relationship between UK and US long-term interest rates in the second part of the chart.

CHART 1.11 **Interest rates**



1.43 In the current target period, February 1983 to April 1984, the growth of £M3 to mid-October was just within the target range of 7–11 per cent; PSL2 and M1 were rather above the top of the range. Since the summer, monetary growth on all three measures has slowed significantly compared with earlier in the target period. Narrower non-interest bearing forms of money continue to grow more slowly than the broader aggregates. The forecast makes the same assumption about 1984–85 as the Medium Term Financial Strategy: that there will be a range for M1, £M3 and PSL2 of 6–10 per cent.

CHART 1.12 **Monetary growth, percentage changes on a year earlier**
for banking months March, June, September and December



Fiscal projections

1.44 The PSBR in 1982–83 was £1½ billion higher than forecast in the FSBR; there was less underspending on central government voted expenditure and higher borrowing by local authorities. The higher level of central government expenditure and higher local authority borrowing seems to have continued into the current financial year. This explains a substantial part of the upward revisions to the anticipated level of public expenditure and the PSBR in 1983–84, despite the cash limit reductions and additional asset sales announced on July 7. In the first seven months of 1983–84, the PSBR was just over £7 billion; the total for the year as a whole is now projected at £10 billion, some £2 billion higher than forecast at Budget time. There is inevitably still a substantial margin of error surrounding this forecast (average errors in PSBR forecasts at this time of year exceed £2 billion) but there are several factors which give grounds for expecting increased public borrowing this year. On the expenditure side the outturn for 1982–83 and information on likely spending this year suggest less shortfall than allowed for in the FSBR. In addition, debt interest payments are higher, partly because of higher borrowing. On revenues, extra receipts from North Sea Oil seem likely to be broadly offset by lower receipts elsewhere.

1.45 The projections in tables 1.7–1.9 take account of the Government's public spending plans shown in part 2. Adopting the conventional assumptions of indexed tax rates, allowances and specific duties and taking a PSBR in 1984–85 of 2½ per cent of GDP, equivalent to £8 billion (as in the MTFS), this points to a negative fiscal adjustment, perhaps of the order of £½ billion. The forecast assumes, conventionally, that the fiscal adjustment takes the form of an increase in income tax. The size of the fiscal adjustment is, of course, extremely uncertain and depends on revenue and expenditure estimates subject to a number of major uncertainties, in either direction. For the public sector as a whole, the flows on either side of the account approach £200 billion.

Expenditure

1.46 General government expenditure in national accounts terms is forecast to rise, in cash, nearly 5½ per cent in both 1983–84 and 1984–85. Table 1.7 shows the basis of these figures.

Table 1.7 General Government Expenditure†

£ billion

	1982–83	1983–84	1984–85
General government expenditure(1)	114	120½	126½
National accounts adjustments(2)	3½	4	5
Interest payments	14	14½	15
Total expenditure in national account terms	**132**	**139**	**146½**

(1) Expenditure on programmes by central government and local authorities plus the contingency reserve and special sales of assets, after making allowance for expected outturn.

(2) Adjustments to line 1 to the definitions used in National Accounts Statistics.

Revenue

1.47 Revenue estimates depend on incomes, spending and prices, as well as on policy decisions. Revenue in 1984–85 is projected on conventional assumptions of revalorisation of the main direct tax allowances and thresholds, and of excise duties, using a figure of 5 per cent*. Estimates for oil revenues assume that North Sea Oil prices do not change very much from present levels.

1.48 The revenue projections are shown in table 1.8. Real GDP (average measure) is forecast to grow by nearly 3 per cent in 1983–84 and 1984–85. The general rate of inflation, as measured by the GDP deflator, is put at about 5 per cent in 1983–84 and 1984–85.

Table 1.8 General Government Receipts†

£ billion

	1982–83	1983–84	1984–85
Taxes on income, expenditure and capital	92	96	104
National Insurance and other contributions	18½	21	22½
Interest and other receipts	11	11	11
Accruals adjustments	—	—	—
Total Receipts	**122**	**128**	**137½**
of which North Sea tax revenues	8	9	9½

Borrowing

1.49 Table 1.9 provides projections of Government receipts, expenditure, and borrowing.

Table 1.9 Public Sector Borrowing†

£ billion

	1982–83	1983–84	1984–85
General government expenditure	132	139	146½
General government receipts	−122	−128	−137½
Implied fiscal adjustment(1)	—	—	−½
General Government Borrowing Requirement	10½	11	8½
Public Sector Borrowing Requirement	9	10	8
as percentage of GDP	3¼	3¼	2½
Money GDP at market prices	282	305	329

(1) On the same assumption as in the 1983 MTFS about the PSBR as a proportion of GDP.

* Part 4 shows the additional direct revenue cost of yields arising from these assumptions, which are reflected in the forecast.

† Totals may not add due to rounding,

The Prospects: summary

Summary

1.50 Table 1.10 presents a summary of the economic prospects.

Table 1.10 Economic Prospects(1)

	Percentage changes 1982 to 1983	1983 to 1984	Average errors(2) from past forecasts
A Output and expenditure at constant 1980 prices			
Gross domestic product (at factor cost)	3	3	1
Consumers' expenditure	3½	2½	1
General government current expenditure	2½	1	1½
Fixed investment	2½	4	2½
Exports of goods and services	½	4	3
Change in rate of stock-building as a percentage of the level of GDP	1	½	1
Imports of goods and services	5	5	3
	1983	1984	
B Balance of payments on current account (£ billion)	½	0	3
C Retail prices index (4th quarter)	5	4½	3(3)

(1) The forecast includes the effect of the fiscal adjustment in 1984–85.

(2) The errors relate to the average differences (on either side of the central figure) between forecast and outturn. The method of calculating these errors has been explained in earlier publications on Government forecasts, notably in the Economic Progress Report, June 1981. The errors are after adjustment for the effects of major changes in fiscal policy, where excluded from the forecast.

(3) The average error for inflation was calculated from a period of much higher inflation and probably overstates the margin of error at low rates of inflation.

Table 1.11 Constant price forecasts of expenditure, imports and gross domestic product*

£ billion at 1980 prices, seasonally adjusted

	Consumers' expenditure	General government consumption	Total fixed investment	Exports of goods and services	Change in stocks	Total final expenditure	Less Imports of goods and services	Less Adjustment to factor cost	Plus Statistical adjustment	Gross domestic product at factor cost	GDP index 1980 = 100
1979	137·9	47·6	41·6	63·3	2·5	292·8	59·9	31·5	1·6	203·0	102·7
1980	136·9	48·4	39·3	63·2	−3·2	284·6	57·7	30·9	1·6	197·6	100·0
1981	137·1	48·3	35·6	61·9	−2·7	280·2	56·3	30·0	0·5	194·4	98·4
1982	138·9	49·0	37·6	62·8	−1·0	287·2	58·0	30·9	−0·4	198·0	100·2
1983	144·0	50·3	38·6	63·1	0·6	296·6	61·0	31·8	−0·3	203·6	103·0
1984	147·6	50·8	40·2	65·7	2·0	306·3	64·2	32·8	0	209·3	105·9
1982 H1	68·4	24·4	18·5	31·6	0·3	143·1	29·5	15·4	0·3	98·5	99·7
H2	70·4	24·7	19·1	31·2	−1·3	144·1	28·5	15·6	−0·7	99·4	100·6
1983 H1	71·4	25·1	19·0	31·5	0·7	147·7	30·1	15·8	−0·6	101·2	102·4
H2	72·6	25·2	19·6	31·6	−0·1	148·9	30·9	16·0	0·3	102·3	103·5
1984 H1	73·1	25·3	20·0	32·5	0·9	151·8	31·7	16·2	0	103·9	105·2
H2	74·5	25·5	20·2	33·2	1·1	154·5	32·5	16·6	0	105·4	106·7
% changes:											
1981 to 1982	1½	1½	6	1½		2½	3	3		2	2
1982 to 1983	3½	2½	2½	½		3½	5	3		3	3
1983 to 1984	2½	1	4	4		3½	5	3		3	3

* GDP figures in the table are based on "compromise" estimates of gross domestic product, reflecting for the past average movements in constant-price expenditure, output and income estimates of GDP. Percentage changes are calculated from unrounded levels and then rounded to half per cent. Totals in £ billion may not add due to rounding. Figures beyond 1983 H1 are forecasts.

2. Outline Public Expenditure Plans for 1984-85

2.01 The Government have reviewed the public expenditure plans for 1984–85 published in the 1983 Public Expenditure White Paper (Cmnd 8789); Table 2.1 shows the revised public expenditure plans as now decided and compares them with the original White Paper plans, and with the plans as modified by the Budget and other changes made before the review. It also shows, for the purposes of comparison, the 1983–84 plans as published in the White Paper, again modified to take account of the Budget and other changes. All figures are in cash unless otherwise stated.

The planning total

2.02 The outcome of the review is to keep the planning total for 1984–85 at the figure in the 1983 White Paper (£126·4 billion) and broadly constant in cost terms compared with 1983–84. Table 2.2 shows the planning totals 1978–79 to 1984–85 in cash and in cost terms; and public expenditure expressed as a ratio to GDP. Full details will be published later in the annual Public Expenditure White Paper.

Changes in plans

2.03 Within the unchanged planning total for 1984–85, increases in some (mainly demand-led) programmes have been substantially offset by savings; there has also been an increase of £0·4 billion in estimated receipts from special sales of assets, reflecting among other factors the fact that the sale of Enterprise Oil is now expected in 1984–85.

Programmes*

Defence

2.04 The provision allows for annual growth of some 3 per cent in real terms, with an addition for Falklands costs.

FCO (including Overseas Development Administration)

2.05 There is an increase of £6 million in provision for the British Council and BBC External Services, largely offset by savings in administration.

European Community

2.06 The estimated net contribution to the Community Budget is that shown in Cmnd. 8789.

Intervention Board for Agricultural Produce

2.07 The increase of £422 million reflects revised estimates of the cost of implementing European Community agricultural support measures.

Agriculture

2.08 The net increase of £15 million mainly reflects estimating increases on expenditure 100 per cent funded by the European Community. Other main changes include adjustments to the capital grants schemes and provision for additional assistance for the horticulture industry and the marginal land areas.

Forestry Commission

2.09 The reduction of £4 million will be mainly achieved by reductions in capital expenditure and overheads.

* Compared with the post-Budget plans.

Trade and Industry

2.10 The provision for 1984–85 is £60 million less than the earlier plans. There are increases in provision for redundant steel and shipbuilding workers, launch aid and industrial research and development. These are more than offset by reductions in Regional Development Grants, reduced provision for support for individual industries and a reduction in the forecast of British Leyland's equity requirement.

Energy

2.11 The main cause of the increase of £86 million is increased support to the coal industry partly offset by small reductions in nuclear R & D and other miscellaneous expenditures.

Export Credits Guarantee Department

2.12 The small increase of £2 million mainly reflects higher estimates of interest support costs for fixed rate export credit.

Employment

2.13 The net reduction of £68 million in 1984–85 reflects savings of £121 million and increases of £53 million. The savings result mainly from new estimates of demand for the Youth Training Scheme, the Job Splitting Scheme and the Young Workers Scheme. The bulk of the increases (£37 million) is accounted for by an extension of the Enterprise Allowance.

Transport

2.14 There is a reduction of £9 million on provision for transport excluding support for nationalised industries. The new towns road programme is nearing completion and there are reduced requirements for ports. There should be scope for higher output on trunk and local authority roads and for some further investment in public transport, provided that price increases do not escalate.

Environment—Housing

2.15 It is proposed that local authority, housing corporation and other gross capital expenditure in the housing field should be set at £3,245 million, almost exactly the same in cash terms as this year's provision. The Secretary of State for the Environment is separately announcing measures to ensure that better use is made of the available provision and particularly of the growing volume of capital receipts from the sale of council houses. These increased receipts, together with other changes, will produce a reduction in the net programme total of £497 million.

Environment—PSA

2.16 An increase of £24 million has been agreed. This is primarily for maintenance of the civil estate, but will also permit some improvements to be made in conditions in Unemployment Benefit Offices.

Environment—Other Environmental Services

2.17 About three-fifths of this programme is local authority current expenditure and has been increased, along with local authority expenditure on other services (see paragraph 2.27). Some reduction has been made in the urban provision for 1984–85 which nonetheless will be higher in cash terms than that for 1983–84.

Home Office

2.18 The net increase of £92 million includes additions of £32 million for prisons and £19 million for police. There is also provision for additional expenditure by the Criminal Injuries Compensation Board and for a start-up loan to the Cable Authority.

Lord Chancellor's Department

2.19 The reduction of £8 million reflects recent underspending on the court building programme.

Education and Science

2.20 Provision is increased by £175 million overall. Four-fifths of the programme is local authority current expenditure. Within other expenditure there is increased provision for the costs of subscriptions to international science; an increase, after higher parental contributions and other savings, in provision for awards for more students in higher education; and savings in certain voluntary and direct grant institutions.

Office of Arts and Libraries

2.21 Total expenditure, which covers both central and local government, is planned to increase by £10 million to £595 million to meet the capital and recurrent needs of the arts, museums and libraries.

Health and Personal Social Services

2.22 The provision for the hospital and community health services should provide growth of nearly 1 per cent for the increasing number of very old people. Cost improvement programmes should release further resources to meet medical advances, reduce treatment shortages and waiting times, and allow other improvements. The provision for capital spending is being increased over this year's level by rather more than the forecast of general inflation. The provision planned for the Family Practitioner Services allows for estimated demand. The provision for personal social services has been increased.

Social Security

2.23 The programme reflects latest estimates of benefit expenditure in 1984–85, including the effect of revised economic assumptions. It provides for an uprating in November 1984 based on the rise in prices in the twelve months to May 1984, although the precise uprating for individual benefits will not be announced until June when the May RPI becomes available. The main policy changes are reductions in the coverage of help with housing costs, particularly housing benefits. The net effect is an increase on previous plans of £163 million.

Scotland, Wales, Northern Ireland

2.24 The net changes in these programmes mainly reflect changes in comparable programmes in England. The Secretaries of State have discretion to make allocations of this comparable expenditure which take account of local factors.

Other departments

2.25 The net increase of £47 million in 1984–85 represents a number of increases and reductions in the expenditure of the tax departments and a large number of small departments.

Nationalised Industries

Nationalised Industries

2.26 External Financing Limits (EFLs) for nationalised industries in 1984–85 are set out in Table 2.3. Overall, there is a decrease of £666 million in expected external financing requirements. Requirements have decreased for all industries, other than the National Coal Board, the British Steel Corporation, British Shipbuilders, and the Civil Aviation Authority.

Local Authorities

Current Expenditure

2.27 In the face of continued overspending the Government have been obliged to increase provision for current expenditure relevant for Rate Support Grant (RSG) for 1984–85 by just under £600 million from the plans underlying Cmnd 8789. Provision will be £24·3 billion. This should enable the Government's policies for individual services to be broadly maintained.

2.28 Local authorities in England and Wales have been given provisional targets for total expenditure based on the revised provision for current expenditure. Guidelines for Scottish local authority current expenditure in 1984–85 will be issued very shortly. Authorities which exceed their targets or guidelines will lose grant. (In 1983–84, some £292 million of grant has been "held back" from authorities in England and Wales in the face of planned overspending; £45 million has been abated from grant in Scotland and four authorities have been required to make rate reductions equivalent to £19 million.)

Exchequer Grants

2.29 Aggregate Exchequer Grant (AEG) in Great Britain before holdback and abatement will be about £14·8 billion. The Government's proposals for AEG in England have already been announced; the Secretaries of State for Scotland and Wales will be making announcements shortly.

Capital Expenditure

2.30 Early returns from the local authorities for 1983–84 suggest no repetition of the massive capital underspending in 1981–82 and 1982–83. Overall, expenditure is expected to be within about £$\frac{1}{4}$ billion of the planned level of just under £4 billion. Some final decisions have yet to be taken on the allocation of programmes for 1984–85, but the plans should provide for local authority capital spending of around £3$\frac{3}{4}$ billion or roughly the same in cash terms as the expected outturn in 1983–84. Some savings have had to be found in the provision for capital spending to help offset authorities' continued overspending on current account. But a measure of end year flexibility is being introduced on the overall cash limits which will permit some carry forward of underspending. The Secretary of State for the Environment is announcing details.

Special Sales of Assets

Special Sales of Assets

2.31 Net proceeds from special sales of assets are shown as increasing by £400 million, reflecting a number of changes, including the postponement of the sale of Enterprise Oil from 1983–84 to 1984–85. There are considerable uncertainties attached to this figure which is dependent on market conditions at the time of sales.

Reserve

Reserve

2.32 The White Paper included for 1984–85 a provisional reserve of £3 billion. In the 1983 review of plans no call has been made on this reserve, which will be available to meet all contingencies including estimating changes. At this stage, the estimates of expenditure in 1984–85 on some demand-led services are inevitably still uncertain.

Table 2.1 Public Expenditure Plans

£ million

	1983–84	1984–85		
	White Paper (Cmnd 8789) with Budget and other pre-survey changes(1)	White Paper (Cmnd 8789)	White Paper (Cmnd 8789) with Budget and other pre-survey changes	Revised plans(2)
Departments (excluding nationalised industries' external finance)(3)				
Ministry of Defence	15 716	17 288	17 270	17 010
Foreign & Commonwealth Office (including Overseas Development Administration)	1 683	1 801	1 806	1 807
European Community	380	450	450	450
Intervention Board for Agricultural Produce	1 274	835	825	1 247
Agriculture	992	998	994	1 009
Forestry Commission	59	60	60	56
Department of Trade and Industry	1 488	1 370	1 411	1 351
Department of Energy	470	457	457	543
Export Credits Guarantee Department	55	164	164	166
Department of Employment	2 981	3 317	3 376	3 308
Department of Transport	3 366	3 466	3 546	3 537
DOE—Housing	2 709	2 988	2 993	2 496
DOE—Property Services Agency	−145	−115	−116	−92
DOE—Other Environmental Services	3 186	3 227	3 210	3 209
Home Office	4 041	4 253	4 241	4 333
Lord Chancellor's Department	449	509	509	501
Department of Education & Science	12 583	12 912	12 877	13 052
Office of Arts & Libraries	560	584	585	595
DHSS—Health and Personal Social Services	14 478	15 382	15 328	15 414
DHSS—Social Security	34 783	35 939	36 687	36 850
Civil Superannuation	937	1 017	1 036	1 053
Scotland(4)	6 160	6 339	6 339	6 318
Wales(4)	2 397	2 486	2 480	2 459
Northern Ireland	3 796	4 019	4 031	4 020
Other Departments	1 967	2 058	2 069	2 116
Adjustment for refund of VAT on certain services contracted out by Government departments	—	—	—	−30
Nationalised industries	2 748	2 615	2 548	1 882
Local authority current expenditure not allocated to departments	904	455	455	625
Special sales of assets	−1 250	−1 500	−1 500	−1 900
Reserve	1 040	3 000	3 000	3 000
PLANNING TOTAL	**119 807**	**126 374**	**127 131**	**126 385**

Note:

(1) Including measures announced on 7 July 1983 and changes of classification.

(2) Some figures may be subject to detailed technical amendment before publication of the 1984 Public Expenditure White Paper.

(3) Provision for pay in these programmes reflects the pay factor of 3 per cent announced on 15 September 1983.

(4) Excluding agricultural expenditure, which is included in the agricultural line.

Public spending 1978–79 to 1984–85

Table 2.2 Public Expenditure Planning Totals 1978–79 to 1984–85

	Planning total £ million		
	Cash(1)	Cost Terms(1,2) base year 1982–83	Public(3) expenditure as % of GDP
1978–79(4)	65 800	106 800	40½
1979–80(4)	76 900	107 000	40½
1980–81(4)	92 700	108 600	42½
1981–82(4)	104 600	111 600	44
1982–83(4)	113 400	113 400	43½
1983–84(5)	119 800	114 100	42½
1984–85(5)	126 400	114 600	42

(1) Figures are rounded to the nearest £100 million.

(2) Cash plans adjusted for general inflation as measured by the GDP deflator at market prices. The GDP deflator is forecast to increase by some 5 per cent in 1983–84 and some 5 per cent in 1984–85 as shown in paragraph 1.48.

(3) Includes planning total plus net debt interest, payments of VAT by local authorities and non-trading government capital consumption.

(4) Outturn/estimated outturn.

(5) Plans.

External Financing Limits

Table 2.3 External Financing Limits for the Nationalised Industries (1984–85)

	£ million(1)
National Coal Board	1103
Electricity (England and Wales)	−740
North of Scotland Hydro-Electric Board	−2
South of Scotland Electricity Board	261
British Gas Corporation	−100
British Steel Corporation	275
British Telecom	−250
Post Office	−52
National Girobank	−1
British Airways Board	−160
British Airports Authority	10
British Railways Board	936
British Waterways Board	43
National Bus Company	66
Scottish Transport Group	16
British National Oil Corporation(2)	−4
British Shipbuilders(3)	175
Civil Aviation Authority	20
Water (England and Wales)	286
Total	**1882**

(1) Figures are shown rounded to the nearest £1 million.

(2) The figure for BNOC is not a limit. BNOC's trading results are likely to fluctuate from year to year given the uncertainties of oil trading.

(3) The British Shipbuilders EFL is provisional pending decisions on the industry's corporate plan.

3. Proposed changes to National Insurance Contributions

3.01 Full Class 1 National Insurance Contribution rates are currently 9·0 per cent for employees and 10·45 per cent for employers. Contributions are payable on all earnings once the lower earnings limit of £32·50 a week is reached up to the upper earnings limit of £235 a week. In addition there is a Treasury Supplement equal to 13 per cent of contributions (before taking account of the rebate for contracted-out contributions).

Proposed changes

3.02 It is proposed to leave these rates unchanged from April 1984. The lower earnings limit will increase to £34·00 a week, in line with the single rate retirement pension, and the upper earnings limit to £250. There will be similar increases to the limits for self-employed contributions. The Treasury Supplement will be reduced to 11 per cent of contributions.

3.03 Full details are set out in the statement by the Secretary of State for Social Services made on 17 November 1983 in connection with the laying of the necessary re-rating Order and the accompanying report by the Government Actuary. The estimated effect on employers and employees of the changes proposed here are shown in a statistical table opposite.

3.04 In accordance with normal practice, the Government Actuary has been provided with working assumptions for the purpose of preparing his report. These assumptions, which are not forecasts or predictions, are summarised in his report, and include the following: that the number unemployed, GB excluding school leavers etc., averages 2,850,000 in 1983–84 and in 1984–85; that average earnings in the tax year 1984–85 will be $6\frac{1}{2}$ per cent higher than in 1983–84; and that the movement in prices between May 1983 and May 1984, which is the relevant period for the November 1984 benefit uprating, will be $5\frac{1}{2}$ per cent.

Table 3.1 Estimated Total Payments in 1983–84 and 1984–85 by Employees and Employers in National Insurance Contributions and National Insurance Surcharge(1)

Great Britain (£ million)

	National Insurance Contributions			NI Surcharge	Total Employees+ Employers contributions +NIS	Total Employers contributions +NIS
	Employees	Employers	Total Employees+ Employers	Employers		
Contributions in 1983–84	9 210	10 310	19 520	1 670	21 200	11980
1984–85 change from increased earnings etc(2)	590	620	1 210	−380(3)	830	240
1984–85 change from increases in earnings limits	70	80	150	10	160	90
Total contributions in 1984–85	**9 880**	**11 010**	**20 890**	**1 300**	**22 190**	**12 310**

(1) Figures are rounded to the nearest £10 million and may not sum. Detailed figures for National Insurance Contributions are included in the Government Actuary's report on the draft of the Social Security (Contributions, Re-rating) Order 1983.

(2) Including population and employment changes.

(3) The net decrease in NIS receipts between 1983–84 and 1984–85 reflects the fact that the rate for local authorities is $2\frac{1}{2}$ per cent throughout 1983–84 and for other employers was $1\frac{1}{2}$ per cent until 1 August, 1983, when it was lowered to 1 per cent. The table assumes that the surcharge remains at 1 per cent for all employers in 1984–85.

Note: As in previous years, figures in this table are on a receipts basis, excluding self-employed and voluntary contributions. Figures include NHS and Employment Protection Allocation contributions. Employers contributions have not been adjusted to take account of deductions in respect of statutory sick pay.

4. The Revenue Effects of Illustrative Tax Changes

4.01 The tables below show various illustrative changes to the major taxes and estimates of their direct revenue effects at forecast 1984–85 price and income levels. Figures are given for full year effects and also the effect in the first year (1984–85)—that is, the part of the full year effect which would be expected to come through in tax receipts in that financial year. Neither of these is the same as the effect on the public sector borrowing requirement (PSBR), because of the second round effects of tax changes on the economy.

4.02 Estimates of the size of the direct effects of tax changes depend on economic variables, such as prices, earnings, consumer expenditure, etc, and thus may alter as the prospects change. The illustrative tables which follow are based on a view of the economy that is consistent with Part 1.

4.03 There are, in principle, a number of ways of measuring the direct effect on revenue of a tax change, depending on the assumptions made about changes in the tax base and whether revenue from other taxes is included. The definitions used here are explained in more detail on page 9 of the 1981–82 Financial Statement and Budget Report.

4.04 Where appropriate the figures set out below show the effect of indexation by an illustrative 5 per cent. This is in line with the annual rate of increase in the RPI forecast for the fourth quarter of this year (table 1.10).

Indexation of allowances, thresholds and bands for 1984-85

4.05 With indexation by 5 per cent, the 1984–85 levels of allowances, thresholds and bands would be as shown below. The rules for rounding up set out in the 1980 Finance Act (for income tax) and the 1982 Finance Act (for capital transfer tax and capital gains tax) have been followed. 1983–84 figures are shown for comparison.

Indexation: Income Tax

Table 4.1 Income Tax

	1983–84	1984–85
Allowances	£	£
Single and wife's earned income allowance	1785	1875
Married allowance	2795	2935
Additional personal and widow's bereavement allowance	1010	1060
Single age allowance	2360	2480
Married age allowance	3755	3945
Aged income limit	7600	8000

Income tax rates	Bands of taxable income	
per cent	1983–84	1984–85
	£	£
30	0–14 600	0–15 400
40	14 601–17 200	15 401–18 200
45	17 201–21 800	18 201–23 100
50	21 801–28 900	23 101–30 600
55	28 901–36 000	30 601–38 100
60	over 36 000	over 38 100

	1983–84	1984–85
	£	£
Investment income surcharge threshold	7100	7500

Indexation: Capital Taxes

Table 4.2 Capital Transfer Tax

Rate on death	Lifetime rate	Bands of chargeable value	
		1983–84	1984–85
per cent	per cent	£'000	£'000
Nil	Nil	0– 60	0– 63
30	15	60– 80	63– 84
35	17½	80– 110	84– 116
40	20	110– 140	116– 147
45	22½	140– 175	147– 184
50	25	175– 220	184– 231
55	30	220– 270	231– 284
60	35	270– 700	284– 735
65	40	700–1325	735–1392
70	45	1325–2650	1392–2783
75	50	over 2650	over 2783

Table 4.3 Capital Gains Tax

	1983–84	1984–85
	£	£
Annual exempt amount		
Individuals	5300	5600
Trusts	2650	2800

Indexation: Costs

4.06 Estimates of the costs of the changes shown above are as follows:

Table 4.4 Costs of Indexation

£ million at forecast 1984–85 prices, incomes and capital values

	First year cost		Full year cost	
Indexation of income tax allowances and thresholds of which:	800		1045	
Increases in main personal allowances		730		900
Increases in the basic rate limit(1)		40		70
Increases in further higher rate thresholds(1)		30		60
Increases in investment income surcharge threshold		Negligible		15
Indexation of capital transfer tax thresholds and bands	15		35	
Indexation of capital gains tax exempt amounts	Nil		10	

(1) Additional costs after previous changes have been introduced.

Direct revenue effects of other illustrative changes in income tax and corporation tax

4.07 Table 4.5 below gives estimates of the direct effects (at forecast levels of 1984–85 prices and incomes) of changes in the main personal allowances, thresholds and rates of *income tax* from the indexed levels of allowances and thresholds set out in table 4.1 above. For *corporation tax* the table shows the effects of a 1 percentage point change in the rate of tax and in the small companies' rate.

Revenue Effects: Income tax

4.08 The income tax changes have been costed on the assumption that each is introduced in isolation. In practice there is little interaction between the personal allowances, so an estimate of the cost of more than one allowance change can be obtained by combining the individual costs or yields for each item. However, the effect of a change in the basic or higher rates of tax, or in the higher rate thresholds, would be smaller than the amounts shown in the table if those changes were introduced at the same time as an increase in one or more allowances (and larger if combined with a decrease in allowances).

4.09 Table 4.5 shows the costs or yields resulting from individual allowance changes of £20 and of changes in all allowances by 1 and 10 per cent of their 1983–84 values. These changes are applied to the indexed levels of table 4.1. The costs or yields are linear over a fairly broad range of changes. Reasonably accurate estimates can be obtained by pro-rating the ready reckoner figures for increases in allowances of less than about 20 per cent and for reductions of less than about 5 per cent from the indexed values. The estimated revenue effects of each allowance and threshold change are shown to the nearest £ million (to avoid undue magnification of rounding errors when using the ready reckoner to consider larger changes). However, the figures should not be assumed to be accurate to this degree.

4.10 The additional cost of an increase in the higher rate thresholds tends to fall as the total increase rises, so estimates have been given for two different changes, 1 per cent and 10 per cent on top of indexation. Nor are the effects of changes in higher rate thresholds symmetrical between increases and decreases. The table indicates that decreases would yield rather more than corresponding increases would cost.

4.11 Changes to the investment income surcharge are independent of the rest of the tax regime. As with the higher rate thresholds, the yield from reducing the investment income surcharge threshold is not the same as the cost of raising it by a corresponding amount. Changes in the threshold are broadly linear for increases of less than about 15 per cent and for decreases of less than about 5 per cent from the indexed values. The effect of a change in the rate of surcharge would be less if the threshold were increased at the same time (and greater if combined with a reduction in the threshold).

Table 4.5 Direct effects of specimen changes in income tax and corporation tax

£ million at forecast 1984–85 income levels

Ready Reckoner: Income Tax

	First year Cost/Yield	Full year Cost/Yield
Income Tax(1)		
Rates		
Change basic rate by 1p(2)	950	1025
Change all higher rates by 1p	35	70
Personal Allowances		
Change single and wife's earned income allowance by £20	63	76
Change married allowance by £20	52	64
Change single age allowance by £20	5	7
Change married age allowance by £20	4	5
Change aged income limit by £100	2	3
Change all main personal allowances by 1 per cent	145	177
Change (raise−/lower+) all main personal allowances by 10 per cent	−1415/+1470	−1735/+1805
Higher Rate Bands		
Change (raise−/lower+) all higher rate thresholds by 1 per cent	−12/+12	−21/+22
Change (raise−/lower+) all higher rate thresholds by 10 per cent	−110/+140	−190/+245
Investment Income Surcharge		
Change (raise−/lower+) threshold by £500	−1/+1	−17/+19
Change rate by 1p	1	19
Allowances and thresholds		
Change all main personal allowances and higher rate and investment income surcharge thresholds by 1 per cent	162	201
Change (raise−/lower+) all main personal allowances and higher rate and investment income surcharge thresholds by 10 per cent	−1575/+1690	−1945/+2090

Ready Reckoner: Corporation Tax

Corporation Tax(3)

£ million

	First year	Full year
Change rate by 1 percentage point(4)	100	170
Change small companies' rate by 1 percentage point	10	18

(1) Changes are from the indexed levels of allowances and thresholds shown in table 4.1. Percentage changes are, however, of 1983–84 levels.

(2) Including the effect of the change on receipts of Advance Corporation Tax and on consequent liability to Mainstream Corporation Tax.

(3) Assessment to Corporation Tax normally relates to the preceding year. These are, therefore, the changes to revenue that would occur if the changed rates were applied to forecast 1983–84 income levels.

(4) Assuming small companies' rate unchanged.

4.12 The effect of a package which changes all main personal allowances and higher rate and investment income surcharge thresholds by 1 per cent and 10 per cent is also shown. These changes have been calculated as percentages of the 1983–84 levels and the effects estimated on top of the 5 per cent illustrative indexation.

4.13 Estimates derived from this ready reckoner for a combination of more than one income tax change should be taken only as a general guide to the revenue effect of the package, particularly where a number of interacting changes are included.

Indirect taxes

4.14 Figures for changes in the excise duties (table 4.6) are shown in two sections. The first shows the extra revenue from the individual duties if they were to be increased by exactly 5 per cent, together with the price increase that would result (after allowing for consequential VAT).

4.15 The second section shows for most duties the revenue yield from changing current levels of duty so that (after VAT) the price of a typical item is changed by exactly one penny. For VED, a £1 change for cars and light vans, and a 1 per cent change for goods vehicles is shown.

4.16 Table 4.7 shows the revenue effects of a 1 percentage point change in the rates of VAT and NIS.

4.17 Within limits the illustrative changes for specific duties shown here can be extrapolated, either up or down, to give a reasonable guide to the revenue effects. For example, a unit change could be combined with a revalorisation change to show the effects of a different percentage movement in duty. However, with large changes the effect on sales and hence on revenue could become significant.

Table 4.6 Revenue effects of indirect tax changes

(£ million 1984–85 prices and income levels)

	5% Revalorisation(1)			Unit changes from present levels of duty		
	Current level of duty on typical item(2)	Price change inc. VAT (pence)	Full year yield(3) £m	Price change inc. VAT	Actual percentage change in duty %	Full year(3) yield/cost £m
Indirect Taxes						
Beer (pint)	15·1p	0·9	80	1p	5·7	95
Wine (bottle of table wine 75 cl)	84·75p	4·9	25	1p	1·0	5
Spirits (bottle)	£4·56	26·2	25	1p	0·2	1
Tobacco (20 kingsize cigarettes)(4)	66·2p	3·3	110	1p	1·5	35
Petrol (gallon)	74·1p	4·3	210	1p	1·2	50
Derv (gallon)	62·83p	3·6	50	1p	1·4	12½
VED (cars and light vans)	£85	£4·25	77	£1	1·2	18
VED (goods vehicles)	£150–£2940	£7·50–£147·00	19	£1·50–£29·40	1·0	3·8

(1) An 'across the board' revalorisation by 5 per cent (including the minor duties not shown above) would yield about £600m in a full year, and the impact on the RPI would be to raise it by less than ½ per cent.

(2) VAT is payable in addition to the duty except in the case of VED.

(3) Assuming for illustrative purposes implementation on 1 April, the first and full-year yield of changes in excise duties would be identical for petrol, derv and VED; for beer and tobacco the first-year yield would be approximately eleven twelfths of the full-year yield; and for wine and spirits it would be approximately twenty-three twenty-fourths.

(4) The duty on cigarettes has *ad valorem* and specific elements; the percentage change relates only to the specific element, but the price change includes the subsequent increase in *ad valorem* duty and VAT.

Table 4.7 VAT and NIS

	First year(1) yield/cost	Full year yield/cost
1% point change in rate of VAT	550	740
1% point change in NIS	1180	1330
assuming recovery from the public sector	750	850

(1) Assuming implementation on 1 April.

Printed in the UK by Her Majesty's Stationery Office
3150888 Dd 402112 C60 11/83
ISBN 0 10 211284 3

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