Financial Statement and Budget Report 1991-92

HM TREASURY
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Gregg

Financial Statement and Budget Report 1991–92

Return to an Order of the House of Commons dated 19 March 1991: for

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Treasury Chambers
19 March 1991 } The Hon. Francis Maude

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Contents

Table 1.1 The Budget measures[1]

	£ million		yield(+)/cost(−)
	1991–92		1992–93
	Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base
Corporation tax			
main rate reduced twice	−380	−380	−830
three-year carry-back of losses	★	★	−250
small companies' limits increased	★	★	−20
National insurance			
employers' contributions on company cars and fuel	—	—	+610
Income tax			
personal allowance and over-65 allowances indexed	−1 635	—	—
other allowances unchanged	—	+360	+490
basic rate limit raised	−470	−140	−240
mortgage interest relief limited to basic rate	+220	+220	+420
full relief for profit-related pay	−35	−35	−60
car benefit scales raised	+190	+190	+250
PAYE and NICs			
small employers allowed to pay quarterly	−210	−210	★
Value added tax			
standard rate raised to $17\frac{1}{2}$ per cent	+3 900	+3 900	+5 515
registration limit raised	−25	−25	−40
waiting period for bad debt relief halved	−190	−190	−50
Excise duties			
tobacco duties raised	+735	+290	+335
alcohol duties indexed	+310	+10	+10
petrol, derv and other oils duties raised	+1 440	+550	+625
vehicle excise duty frozen	—	−270	−280
pool betting duty rate reduced	−15	−15	−20
Other tax changes	+340	+385	−35
Total central government receipts	**+4 175**	**+4 640**	**+6 430**
Community charge reduced	−4 345	−4 345	−4 540
Child benefit raised[2]	...	...	...
Total general government receipts	**−170**	**+295**	**+1 890**

[1] *The tax, national insurance and community charge measures, and the basis of the costings shown, are described in more detail in Chapter 4.*
[2] *See Chapter 5. Public expenditure costs of around £220 million in 1991–92 and £450 million in 1992–93 will be met from the Reserve.*

— = *Nil.*
★ = *Negligible.*
... = *Not applicable.*

1 The Budget

1.01 The objectives of the Government's economic policy are to defeat inflation and to promote output growth and the creation of jobs.

1.02 The Financial Statement and Budget Report (FSBR) supplements the Chancellor's Budget Statement. It presents the Medium Term Financial Strategy (MTFS); describes developments in the economy over the past year and provides economic forecasts to mid-1992; sets out the Budget proposals; summarises the Government's spending plans; and gives forecasts for the public finances for the year ahead.

The Medium Term Financial Strategy

1.03 Chapter 2 describes the framework within which the Government will pursue its objective of defeating inflation. Monetary policy will be conducted so as to sustain sterling's position within its Exchange Rate Mechanism (ERM) bands. This will ensure that UK inflation moves progressively into line with the best inflation performance elsewhere in the ERM. The Government is retaining a target range for narrow money (M0) to underpin its ERM commitment; and will continue to monitor broad money carefully. ERM membership does not change the need for monetary policy to be supported by a firm fiscal policy; it remains the Government's objective to balance the budget over the medium term, which means a borrowing requirement at low points in the cycle and a debt repayment at high points. Given the current stage of the cycle the budget is expected to move temporarily into deficit before returning to balance in the medium term.

The economy

1.04 Chapter 3 describes the main developments in the economy in 1990 and the prospect to mid-1992. The economy went into recession in the second half of last year after some years of exceptionally strong growth. Activity is likely to remain weak in early 1991 before starting to recover in the second half of the year; output for the year as a whole may be 2 per cent lower than in 1990. Retail price inflation has fallen nearly 2 per cent from its peak in October 1990. It is expected to fall sharply through this year, to 4 per cent by the fourth quarter, with a further fall to $3\frac{3}{4}$ per cent by mid-1992.

Budget measures

1.05 Chapter 4 sets out the tax, national insurance and community charge proposals in the Budget. The community charge is to be reduced by £140, and the standard rate of VAT increased to $17\frac{1}{2}$ per cent. The rate of corporation tax will come down from 35 per cent to 33 per cent in two stages, and there are various measures to help small firms; the total help to business in 1991–2 is more than £$\frac{3}{4}$ billion. Employers are to pay national insurance contributions on the private benefit of cars provided for their employees, with the first payment due in June 1992. The income tax personal allowance and age-related allowances are indexed; the basic married couple's allowance is unchanged. Child benefit is increased. Mortgage interest relief is limited to the basic rate, and the basic rate limit is raised by £1 000 more than indexation. Excise duties on tobacco and fuel are raised by 15 per cent, alcohol duties are indexed and vehicle excise duties are frozen. Table 1.1 summarises the direct effects of these measures on the public finances.

Public expenditure **1.06** Chapter 5 sets out the Government's spending plans to 1993–94. The planning total from 1991–92 onwards has been increased to allow for the additional support for local authorities to finance the reduction in the community charge. These increases in the planning total will be offset by lower self-financed expenditure by local authorities, and so will not add to total general government expenditure. The increase in child benefit will be charged to the Reserve. This chapter also provides the latest estimate of outturn for the planning total in 1990–91.

Public sector finances **1.07** Chapter 6 presents the complete financial picture for the public sector. A public sector debt repayment of £$\frac{3}{4}$ billion is forecast for 1990–91. For 1991–92, the forecast is for a public sector borrowing requirement of £8 billion. Table 1.2 shows the main components of general government receipts and expenditure.

Table 1.2 The finances of the public sector[1]

	£ billion 1990–91 1990 Budget[6]	1990–91 Latest estimate	1991–92 Forecast
RECEIPTS			
Inland Revenue:			
Income tax	55·0	55·5	59·6
Corporation tax[2]	20·7	21·6	19·5
Petroleum revenue tax	1·1	0·9	0·0
Capital gains tax	2·1	1·9	1·4
Inheritance tax	1·2	1·3	1·3
Stamp duties	1·9	1·7	2·1
Total Inland Revenue	**81·9**	**82·9**	**83·9**
Customs and excise:			
Value added tax	32·1	30·8	35·7
Petrol, derv duties etc.	9·7	9·6	10·9
Tobacco duties	5·4	5·6	6·1
Alcohol duties	4·9	4·9	5·2
Betting and gaming duties	1·0	1·0	1·1
Car tax	1·5	1·4	1·3
Customs duties	1·9	1·7	1·7
Agricultural levies	0·1	0·1	0·2
Total Customs and Excise	**56·7**	**55·3**	**62·2**
Vehicle excise duties	3·0	3·0	3·0
Oil royalties	0·7	0·6	0·5
Rates[3]	12·2	12·2	14·4
Other taxes and royalties	3·2	3·5	3·8
Total tax and royalty receipts[4]	**157·7**	**157·5**	**167·6**
Social security receipts[4]	35·4	34·9	36·7
Community charge receipts[4]	11·2	10·4	7·6
Interest and dividends	6·4	6·4	6·1
Gross trading surpluses and rent	3·0	3·4	3·3
Other receipts[5]	4·9	4·0	5·1
General government receipts	**218·6**	**216·6**	**226·5**

	£ billion 1990–91 1990 Budget[6]	1990–91 Latest estimate	1991–92 Forecast
EXPENDITURE			
Central government expenditure	**138·7**	**140·6**	**152·1**
of which:			
Social security	52·0	51·8	58·2
Health and OPCS	22·1	22·5	24·9
Defence	21·2	22·1	22·8
Scotland	4·9	4·9	5·8
Wales	2·3	2·2	2·5
Northern Ireland	5·9	5·9	6·4
Other departments	30·4	31·9	31·5
Overseas contributions to costs of Gulf conflict	—	−0·7	
Central government support for local authorities	**41·8**	**42·6**	**52·5[7]**
Financing requirements of nationalised industries	**0·5**	**2·5**	**2·3**
Privatisation proceeds	**−5·0**	**−5·3**	**−5·5**
Reserve	**3·0**	**—**	**3·5**
Planning total	**179·0**	**180·4**	**205·0**
Local authority self financed expenditure[8]	13·3	14·7	9·1
Central government debt interest	17·0	17·6	16·7
Accounting adjustments	3·4	3·4	3·9
General government expenditure	**212·7**	**216·0**	**234·8**

Expenditure, receipts and borrowing

	£ billion 1990–91 1990 Budget	1990–91 Latest estimate	1991–92 Forecast
General government expenditure	212·7	216·0	234·8
General government receipts	218·6	216·6	226·5
General government borrowing requirement	−5·9	−0·5	8·3
Public corporations' market and overseas borrowing	−1·0	−0·3	−0·4
Public sector borrowing requirement	**−6·9**	**−0·8**	**7·9**

[1] *In this and other tables constituent items may not add up to totals because of rounding.*
[2] *Includes advance corporation tax (net of repayments):* 7·5 7·6 7·9
— also includes North Sea corporation tax after ACT set off and corporation tax on gains.
[3] *Local authority rates and national non-domestic rates.*
[4] *On a receipts basis. See Annex to Chapter 6.*
[5] *Includes accruals adjustment to index linked gilts.*
[6] *On current definitions.*
[7] *Includes additional support for local authorities to finance reduction in the community charge. See Chapter 5.*
[8] *See footnote 3 to Table 5.1.*

2 The Medium Term Financial Strategy

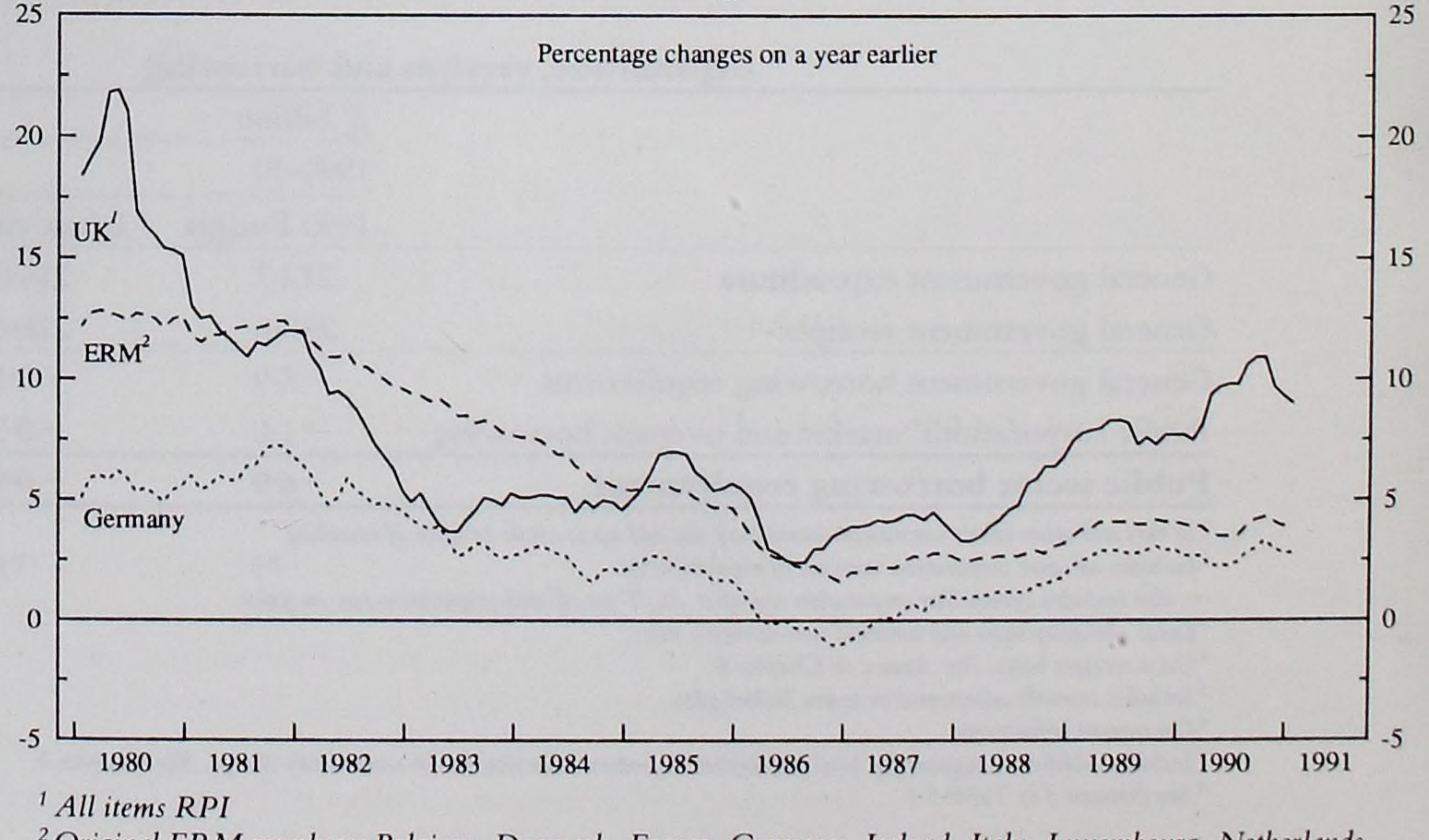
2.01 The central objective of the Government's macroeconomic policy continues to be the defeat of inflation. Low inflation is an essential precondition for healthy economic performance and the success of other policies aimed at improving the flexibility and efficiency of markets.

The policy framework

2.02 The UK joined the Exchange Rate Mechanism (ERM) of the European Monetary System on 8 October 1990 with wide (6 per cent) bands around sterling's central rates against other participating currencies. Interest rates remain the essential instrument of monetary policy, but now the overriding factor in setting them is the need to meet the UK's ERM obligations.

2.03 Sustaining sterling's position within its ERM bands will secure lower inflation in the UK. The operation of the ERM encourages convergence on low rates of inflation. All members are committed to low inflation, and those countries with the lowest inflation effectively set the pace for the others. Monetary policy has to be relatively tight in countries with above average rates of inflation and relatively weak currencies. Thus the UK's inflation rate can be expected to move progressively into line with the best inflation performance elsewhere in the ERM.

Chart 2.1 UK, German and ERM consumer price inflation



[1] *All items RPI*

[2] *Original ERM members: Belgium, Denmark, France, Germany, Ireland, Italy, Luxembourg, Netherlands*

2.04 The speed at which inflation falls will depend on the stance of policy both in the UK and elsewhere in Europe, and on the pace at which markets adjust to the new monetary policy framework. Employers and employees will need to take account of wage settlements in other countries within the ERM. The quicker the growth of labour costs moderates, the sooner the UK will be able to combine low inflation with a satisfactory rate of growth of output.

2.05 ERM membership does not change the need to support monetary policy with a firm fiscal stance. The Government will continue to aim for a balanced budget over the medium term, while permitting some fluctuation in the PSBR over the cycle.

2.06 The following sections explain the Government's approach to monetary and fiscal policy within the ERM, and set out fiscal projections over the medium term based on illustrative paths for money GDP, real output, and inflation.

Monetary policy

2.07 Membership of the ERM sets a new framework for monetary policy. Interest rate decisions must now be set consistently with keeping sterling within its announced bands. This commitment is accordingly a constraint upon the relationship between UK interest rates and those in other ERM countries. Interest rate convergence will follow inflation convergence. Both are likely to take some time to achieve.

Assessment of monetary conditions

2.08 Like all the other larger countries within the ERM, the Government will continue to set a monetary target, and to take account of a range of other indicators of domestic monetary conditions. This approach helps to ensure that the ERM as a whole has a firm nominal anchor.

2.09 There may be occasions when tensions arise between domestic conditions and ERM obligations, with domestic conditions pointing to interest rate levels either higher or lower than those indicated by ERM obligations. But such occasions are expected to be the exception rather than the rule and to be relatively short lived. The experience of other ERM countries suggests that external and domestic considerations will more often point in the same direction. Any loss of discretion to respond to domestic monetary conditions is likely to be more than compensated for by the improved market confidence and reduced inflationary expectations that the ERM commitment is bringing about.

Narrow money

2.10 Narrow money (M0) has been a reliable indicator of monetary conditions, picking up both the unexpectedly buoyant demand conditions in the first half of 1990 and the sharp turnaround in the economy in the late spring and early summer. For 1990–91 as a whole M0 is now forecast to have increased by 4·6 per cent, within the 1 to 5 per cent target range set a year ago. The Government proposes to set a target for M0 for the financial year 1991–92: the target range will be 0 to 4 per cent, the same as the illustrative range for 1991–92 shown in last year's MTFS, and a 1 percentage point reduction on the 1990–91 target range. Growth of M0 within this range will help to underpin the Government's ERM commitment.

Broad money and credit 2.11 The UK has set no target for broad money for the past four years. Over this period the velocity of broad money has not been sufficiently predictable to justify reintroducing a target for it. But the Government will continue to monitor M4 and the other broad aggregates carefully.

Funding policy 2.12 Over the past year the Government has continued to follow the "full fund" rule which was discussed in detail in Annex A to last year's MTFS. With the reduction in the PSDR in 1990–91 funding was resumed towards the end of the financial year. The £8 billion PSBR forecast for 1991–92, together with gilt-edged redemptions of over £6 billion falling due in the year, will involve a return to gilt sales on a larger scale than for the past three years.

Fiscal policy and projections

2.13 The public finances have now returned close to balance, following the surpluses enjoyed since 1987–88. For 1990–91 a net repayment of £$\frac{3}{4}$ billion is now expected, compared with £8 billion in 1989–90. This reduction reflects the fall in output: non-North Sea output is now expected to have fallen by $\frac{1}{2}$ per cent between 1989–90 and 1990–91.

Fiscal policy 2.14 The Government's objective is to balance the budget over the medium term. This is a clear and simple rule which ensures that a prudent fiscal policy supports monetary policy in the fight against inflation. It implies that the ratio of net public debt to GDP, and hence the burden of debt interest payments, will continue on a downward trend; and also provides scope for the burden of taxation to fall over the medium term as public expenditure declines as a share of GDP.

2.15 Cyclical variations in public sector borrowing and debt repayment are consistent with this medium term approach to fiscal policy. The operation of the "automatic stabilisers" implies a borrowing requirement at low points in the cycle and a debt repayment at high points. Public expenditure is affected by changes in economic activity: for example, social security payments change with the level of unemployment. Tax revenues vary more than proportionately with incomes: for certain taxes marginal tax rates exceed average rates. Corporation tax receipts are subject to particularly wide swings. Such variations in the PSBR can be helpful in damping transitory demand changes: they do not involve short term changes to fiscal instruments with the accompanying risk of ill-timed judgements; and they are consistent with a sound underlying fiscal position.

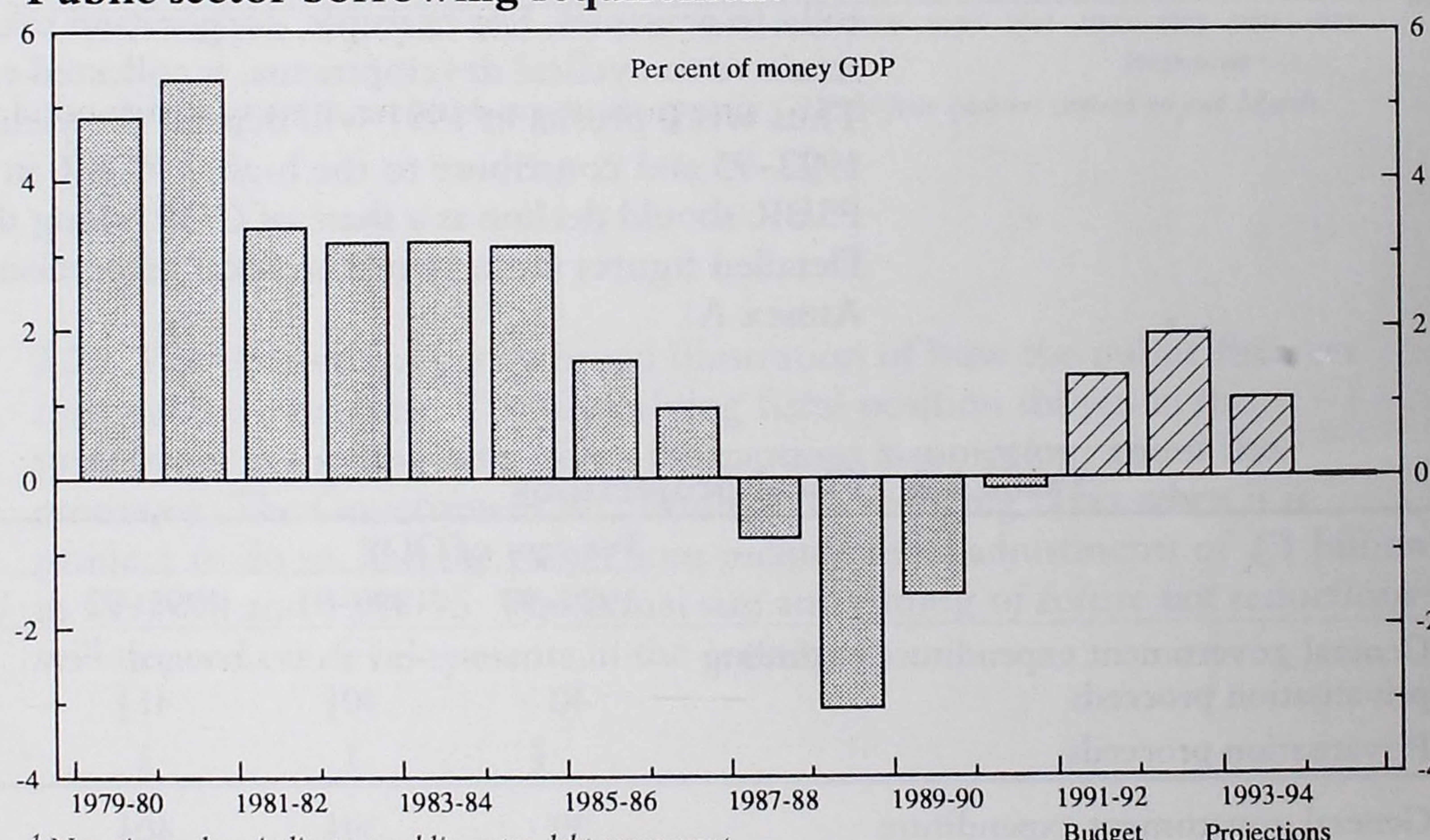
2.16 There has been a clear cyclical pattern in the public finance over many years. The public sector moved into substantial surplus during the years of very rapid growth between 1985 and 1988, with the PSDR reaching 3 per cent of GDP in 1988–89. Since then, as the economy has slowed down, the surplus has declined and the present position is one of broad balance.

2.17 The public sector is now expected to move temporarily into deficit, reflecting the cyclical downswing in the economy. However, as inflation comes down and output recovers, the budget will return to its underlying balance.

The PSBR in 1991–92

2.18 The PSBR has been set at £8 billion for 1991–92, equivalent to about $1\frac{1}{4}$ per cent of GDP. This is consistent with the objective of balancing the budget over the cycle.

Chart 2.2 Public sector borrowing requirement[1]



[1] *Negative values indicate a public sector debt repayment*

The economy in the medium term

2.19 Assumptions about path of the economy are required in order to illustrate possible developments in the public finances over the medium term. Table 2.1 shows the economic assumptions which form the basis for the fiscal projections set out in Table 2.2.

2.20 The money GDP path after 1991–92 is a stylised projection compatible with the adjustment of the UK economy within the ERM. Over the medium term inflation is shown falling to 3 per cent, which is assumed to be close to performance in the main ERM countries. The level of real GDP will be below trend in 1991–92. But as inflation moderates real GDP growth is likely to recover, and there should be scope for above trend output growth for a while without arresting progress on inflation.

Table 2.1 Money GDP growth, output growth and inflation[1]

	1990–91[2]	1991–92[3]	1992–93	1993–94	1994–95
Money GDP	**7¼**	**6**	**7½**	**7**	**6¼**
Real GDP:					
Non-North Sea	−½	−1	2¾	3	3
Total	−½	−1	3	3¼	3¼
Inflation:					
GDP deflator	7¾	7	4½	3¾	3

[1] *Percentage changes on previous financial year; forecasts for 1991–92 and assumptions thereafter.*
[2] *Figures for money GDP growth and the GDP deflator adjusted for distortion arising from the abolition of domestic rates.*
[3] *The Budget increase in VAT adds about 1 per cent to money GDP and the GDP deflator in 1991–92.*

Fiscal projections **2.21** The increase in the PSBR in 1992–93 is consistent with this assumed path of output. It takes time for the effects of low activity to feed through fully to revenues. For example, corporation tax, which is particularly sensitive to cyclical developments, is collected roughly a year in arrears. Thus weak profits in 1991 will depress the yield of corporation tax in 1992–93 and contribute to the higher PSBR in that year. Thereafter the PSBR should decline as a share of GDP, along the lines shown in Table 2.2. Detailed figures underlying the fiscal projections in Table 2.2 are set out in Annex A.

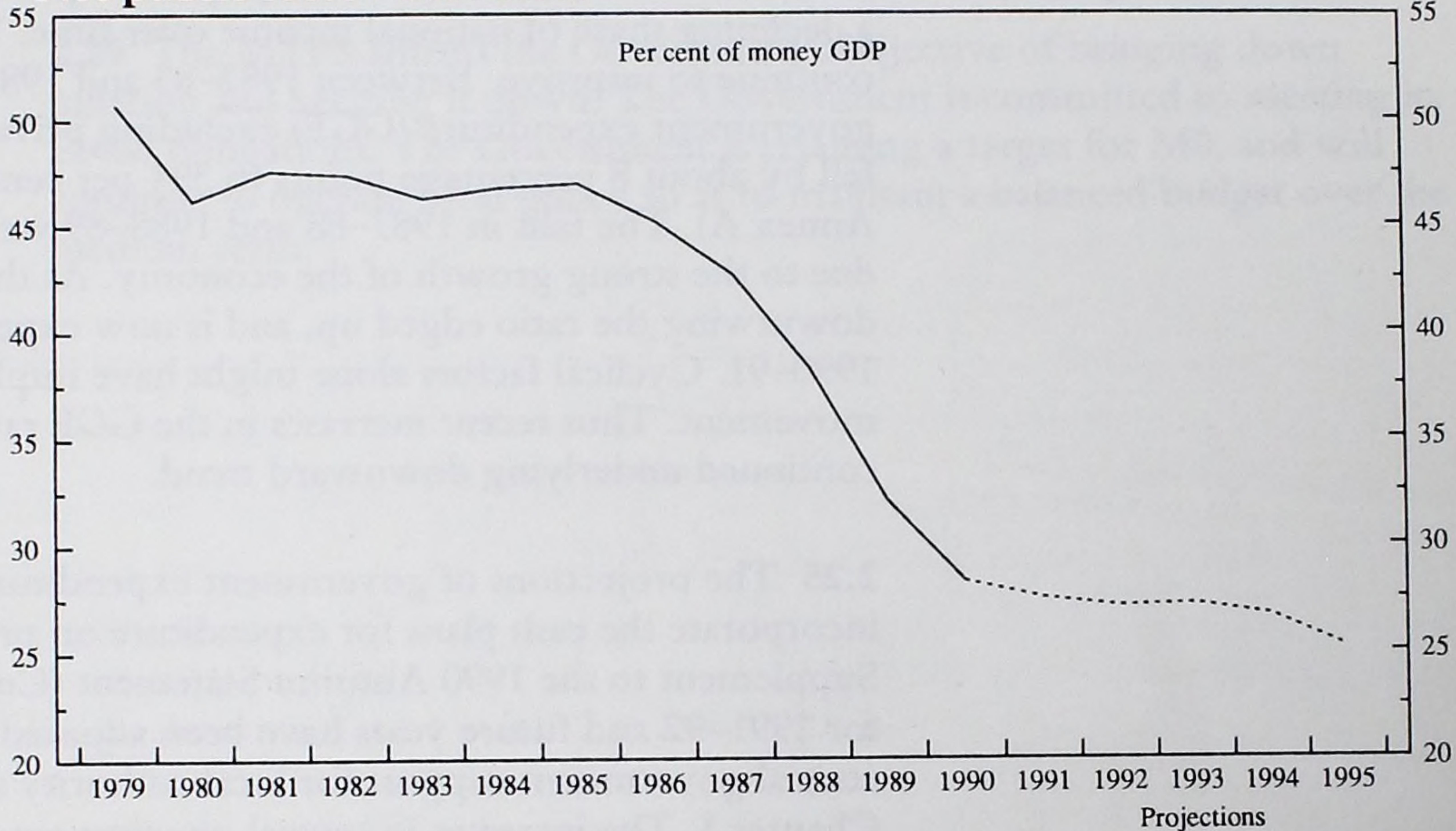
Table 2.2 Fiscal projections[1]

	Per cent of GDP					
	1989–90	1990–91	1991–92	1992–93	1993–94	1994–95
General government expenditure excluding privatisation proceeds	40	40½	41½	41¼	40¾	40
Privatisation proceeds	¾	1	1	1	¾	¾
General government expenditure	39	39½	40½	40½	39¾	39¼
General government receipts	40½	39½	39	38½	39	39½
Cumulative fiscal adjustment[2]	—	—	—	0	¼	¼
Public corporations market and overseas borrowing	−¼	0	0	0	0	0
PSBR	**−1½**	**−¼**	**1¼**	**2**	**1**	**0**
Money GDP at market prices (£ billion)[3]	509·9	547	580	624	668	710

[1] *Rounded to nearest ¼ per cent of GDP.*
[2] *See Table 2A.5 and footnote 2 to that table.*
[3] *Rounded to nearest £1 billion from 1990–91 onwards, and adjusted in 1989–90 to remove the distortion caused by the abolition of domestic rates.*

2.22 The Government's medium term policy of balancing the budget implies that the ratio of net public sector debt to GDP will continue to decline, further reducing the share of the nation's stock of savings absorbed by the public sector. The relatively large PSBR in 1992–93 probably implies a very small rise in the debt ratio. But over the medium term the projections are consistent with a further fall, albeit at a slower rate than over a complete cycle.

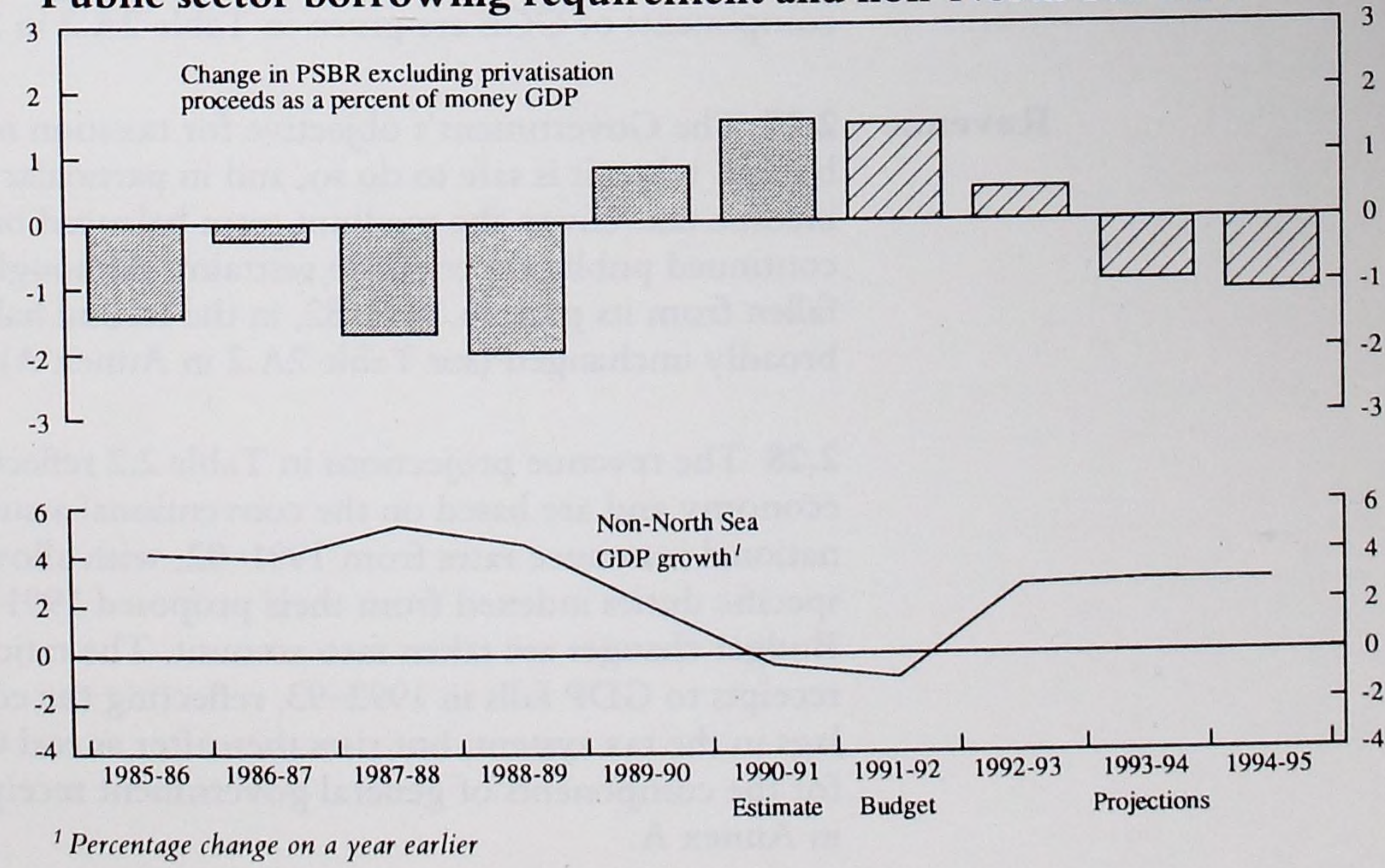
Chart 2.3 Net public sector debt ratio[1]



[1] *Net public sector debt at end March as a percent of money GDP in four quarters centred on end March*

2.23 The projections give a broad illustration of how the public finances may evolve over time. The underlying fiscal position shown in the projections is a strong one, given the cautious assumptions about the economy. The Government is committed to reducing taxes when it is prudent to do so, and the projections include fiscal adjustments of £1 billion in 1993–94 and 1994–95. The actual size and timing of future tax reductions will depend on developments in the economy.

Chart 2.4 Public sector borrowing requirement and non-North Sea GDP



[1] *Percentage change on a year earlier*

Public expenditure

2.24 The Government intends that public spending should continue to take a declining share of national income over time. Value for money should continue to improve. Between 1982–83 and 1988–89 the ratio of general government expenditure (GGE) excluding privatisation proceeds to GDP fell by about 8 percentage points to $39\frac{1}{2}$ per cent (see Table 2A.1 in Annex A). The falls in 1987–88 and 1988–89 were particularly sharp, in part due to the strong growth of the economy. As the economy entered a cyclical downswing the ratio edged up, and is now expected to be $40\frac{1}{2}$ per cent in 1990–91. Cyclical factors alone might have implied a larger upward movement. Thus recent increases in the GGE ratio have taken place around a continued underlying downward trend.

2.25 The projections of government expenditure for the period to 1993–94 incorporate the cash plans for expenditure on programmes published in the Supplement to the 1990 Autumn Statement (Cm 1520). The planning totals for 1991–92 and future years have been adjusted to accommodate increased central government support for local authority spending, as explained in Chapter 5. The increases in central government support to finance the reduction in the community charge are offset by reductions in the projections of local authorities' self-financed expenditure, with no net effect on GGE. The projections of local authorities' self-financed expenditure have also been revised to take account of more recent information on local authorities' actual and planned spending. The new projections of gross debt interest payments and accounting adjustments are consistent with the latest economic assumptions. Further explanation of the GGE projections to 1993–94 is given in Chapter 5. For 1994–95 it is provisionally assumed that GGE will grow by $1\frac{3}{4}$ per cent in real terms: expenditure plans will be settled in future Surveys.

2.26 The projections imply that the ratio of GGE excluding privatisation proceeds to GDP increases in 1991–92, before resuming its downward path from 1992–93 onwards. This profile is broadly as might be expected given the assumptions about the path of output, with the level of real GDP at the trough of its cycle in 1991–92 and recovering thereafter. Projections for the components of GGE are given in Table 2A.3 in Annex A.

Revenue

2.27 The Government's objective for taxation is to bring down the tax burden when it is safe to do so, and in particular to reduce the basic rate of income tax. Given the medium term balanced budget objective this requires continued public expenditure restraint. Although the ratio of tax to GDP has fallen from its peak in 1981–82, in the second half of the 1980s it remained broadly unchanged (see Table 2A.2 in Annex A).

2.28 The revenue projections in Table 2.2 reflect the assumed path of the economy and are based on the conventional assumption of constant tax and national insurance rates from 1991–92, with allowances, thresholds and specific duties indexed from their proposed 1991–92 levels. All proposed Budget changes are taken into account. The ratio of general government receipts to GDP falls in 1992–93, reflecting the economic cycle and payment lags in the tax system, but rises thereafter as real GDP recovers. Projections for the components of general government receipts are given in Table 2A.4 in Annex A.

Summary

2.29 The MTFS affirms the Government's objective of bringing down inflation and keeping it down. The Government is committed to meeting its ERM obligations. The Government is retaining a target for M0, and will continue to operate fiscal policy so as to maintain a balanced budget over the medium term.

Annex A to Chapter 2

Details of fiscal projections and historical data on government expenditure and tax burden.

Table 2A.1 General government expenditure (excluding privatisation proceeds) as a per cent of money GDP[1, 2]

1963–64	36¾	1974–75	48¾	1985–86	45¼
1964–65	36½	1975–76	49¼	1986–87	44
1965–66	37¾	1976–77	46¾	1987–88	42
1966–67	39½	1977–78	43¼	1988–89	39½
1967–68	43¼	1978–79	44	1989–90	40
1968–69	41½	1979–80	44	1990–91	40½
1969–70	41	1980–81	46½		
1970–71	41¼	1981–82	47¼	1991–92	41½
1971–72	41¾	1982–83	47½	1992–93	41¼
1972–73	41¾	1983–84	46½	1993–94	40¾
1973–74	43½	1984–85	46¾	1994–95	40

[1] *1990–91: latest estimate; 1991–92: forecast; 1992–93 onwards: MTFS projections.*
[2] *Based on money GDP figures adjusted for the years before 1990–91 to remove the distortion caused by the abolition of domestic rates.*

Table 2A.2 Non-North Sea taxes, social security contributions and the community charge as a per cent of non-North Sea money GDP[1,2]

1963–64	29½	1974–75	36¼	1985–86	37½
1964–65	30	1975–76	36¾	1986–87	37¾
1965–66	31¾	1976–77	36½	1987–88	38¼
1966–67	32½	1977–78	35½	1988–89	37½
1967–68	34	1978–79	34¾	1989–90	37¾
1968–69	35¾	1979–80	35½	1990–91	37¾
1969–70	37½	1980–81	36¾		
1970–71	37	1981–82	39¼	1991–92	37
1971–72	35¼	1982–83	38¾	1992–93	36¾
1972–73	33	1983–84	38¼	1993–94	37
1973–74	33¾	1984–85	38¼	1994–95	37½

[1] *1990–91: latest estimate; 1991–92: forecast; 1992–93 onwards: MTFS projections (after fiscal adjustment).*
[2] *Based on non-North Sea money GDP figures adjusted for the years before 1990–91 to remove the distortion caused by the abolition of domestic rates.*

Table 2A.3 General government expenditure[1]

	£ billion					
	1989–90	1990–91	1991–92	1992–93	1993–94	1994–95
Public expenditure planning total	162·9	180	205	221	232	243
Local authorities' self-financed expenditure[2]	14·5	14½	9	9½	11½	13
Central government debt interest	17·8	17½	16½	17	17½	17½
Accounting adjustments	4·2	3½	4	5	5½	6
General government expenditure[3, 4]	**199·4**	**216**	**235**	**252**	**266**	**279**
Privatisation proceeds	4·2	5½	5½	5½	5½	5½
General government expenditure excluding privatisation proceeds	**203·6**	**221**	**240**	**258**	**272**	**285**

[1] *For 1989–90 to 1993–94 the figures are taken from Chapter 5.*
[2] *See footnote 3 to Table 5.1.*
[3] *General government expenditure (including and excluding privatisation proceeds) and the public expenditure planning total are rounded to the nearest £1 billion from 1990–91 onwards; local authorities' self-financed expenditure, debt interest, accounting adjustments and privatisation proceeds are rounded to the nearest £½ billion. General government expenditure excluding privatisation proceeds is assumed to grow by 1¾ per cent in real terms in 1994–95.*
[4] *General government expenditure includes debt interest payments to other sectors as follows (£ billion):*

1989–90	*18½*	*1992–93*	*17*
1990–91	*18*	*1993–94*	*17½*
1991–92	*17*	*1994–95*	*18*

Table 2A.4 General government receipts[1]

	£ billion					
	1989–90	1990–91	1991–92	1992–93	1993–94	1994–95
Taxes on incomes, expenditure and capital[2]	158·2	171	177	188	204	219
Social security contributions	33·4	35	37	40	44	48
Interest and dividends	7·2	6	6	6	6	7
Other receipts	7·1	4	6	6	7	7
General government receipts[3]	**206·0**	**217**	**226**	**240**	**260**	**281**
of which North Sea revenues	2·4	2	1	1	2	2

[1] *Taxes and social security contributions are measured on an accruals basis. Accruals adjustments are included in other receipts. Thus total general government receipts are measured on a cash basis.*
[2] *Includes the community charge.*
[3] *General government receipts, and its components, are rounded to the nearest £1 billion from 1990–91 onwards.*

Table 2A.5 Public sector borrowing requirement[1]

	£ billion					
	1989–90	1990–91	1991–92	1992–93	1993–94	1994–95
General government expenditure	199·4	216	235	252	266	279
General government receipts	206·0	217	226	240	260	281
Fiscal adjustment from previous years	—	—	—	—	0	1
Annual fiscal adjustment[2]	—	—	—	0	1	1
GGBR	**−6·6**	**−1**	**8**	**12**	**7**	**0**
Public corporations' market and overseas borrowing	−1·4	0	0	0	0	0
PSBR	**−7·9**	**−1**	**8**	**12**	**7**	**0**
Money GDP[3]	509·9	547	580	624	668	710
PSBR as per cent of money GDP	**−1½**	**−¼**	**1¼**	**2**	**1**	**0**

[1] *Rounded to the nearest £1 billion from 1990–91 onwards. Further details for 1991–92 are provided in Tables 1.2 and 6.9.*
[2] *Means lower taxes or higher expenditure than assumed in lines 1 and 2.*
[3] *Figure for 1989–90 adjusted for the distortion caused by the abolition of domestic rates.*

Annex B to Chapter 2

Changes since the 1990 MTFS

2B.1 Membership of the ERM means that the exchange rate now occupies a central position in the conduct of policy. It will provide a powerful impetus to bring UK inflation down to the best levels attained in the European Community. Developments and policies in other ERM countries will accordingly influence the path of UK money GDP, but in a way that can be expected to contribute to the achievement of the domestic objective of policy. The medium term money GDP projections in this year's MTFS illustrate how that process might evolve.

Narrow money

2B.2 The twelve month growth rate of M0 has been within the target range of 1 to 5 per cent set in last year's MTFS since August 1990; and M0 growth for 1990–91 as a whole is expected to fall within this range. The target range of 0 to 4 per cent set for 1991–92 is the same as the illustrative range for 1991–92 shown in last year's MTFS.

Table 2B.1 Growth of M0

	Percentage changes on a year earlier	
	1990–91	1991–92
1991 MTFS	4·6	0 to 4
1990 MTFS	1 to 5	0 to 4

Money GDP, output and inflation

2B.3 The growth of money GDP is expected to be somewhat lower in both 1990–91 and 1991–92 than envisaged in last year's MTFS, reflecting higher inflation and lower output in both years. The inflation figure in 1991–92 in part reflects the increase in VAT in the Budget, which adds about 1 per cent to the GDP deflator. Output in 1991–92 is now forecast to be much lower than the assumption in the 1990 MTFS. This year's medium term projections for money GDP show it growing somewhat faster than in the medium term objectives set out in the 1990 MTFS, reflecting the changed path of output and the assumed path of inflation convergence within the ERM.

Table 2B.2 Money GDP growth, output growth and inflation

	Differences from 1990 MTFS projections, percentage points			
	1990–91[1]	1991–92	1992–93	1993–94
Money GDP	$-\frac{1}{4}$	$-\frac{3}{4}$	$+1\frac{1}{4}$	$+1\frac{1}{4}$
Real GDP:				
Non-North Sea	$-1\frac{1}{2}$	-3	0	$+\frac{1}{4}$
Total	$-1\frac{1}{2}$	-3	$+\frac{1}{4}$	$+\frac{1}{2}$
Inflation:				
GDP deflator	$+1\frac{1}{4}$	$+2\frac{1}{4}$	$+1$	$+\frac{3}{4}$

[1] *On basis of money GDP growth and GDP deflator figures adjusted for distortion arising from the abolition of domestic rates.*

Fiscal projections 2B.4 Table 2B.3 shows changes in the fiscal projections since the 1990 FSBR. Additional information on 1990–91 is given in Table 1.2 in Chapter 1 and in Chapter 6.

Expenditure 2B.5 The planning total outturn in 1990–91 is discussed in Chapter 5. The cash general government expenditure figures for the future have been revised up since last year.

Receipts 2B.6 Revenues in 1990–91 are expected in total to be lower than forecast in the 1990 FSBR. Latest estimates indicate higher than forecast income and corporation tax receipts, but lower VAT receipts reflecting lower than forecast demand. Social security contributions are also lower than forecast, as are community charge receipts and other receipts. Revenues over the next two years will be affected by the lower level of output than assumed in the 1990 MTFS.

Table 2B.3 **Revenue and expenditure**[1]

	Changes from 1990 MTFS projections, £ billion				
	1989–90	1990–91	1991–92	1992–93	1993–94
1 General government expenditure	**+1½**	**+3½**	**+9½**	**+14**	**+16**
Receipts[2]					
2 North Sea taxes	0	−½	−1½	−1½	−1
3 Other taxes and contributions	+1	+½	0	+3	+9
4 Other[3]	+1½	−2	−1½	−1½	−1½
5 General government receipts	**+2½**	**−2**	**−3**	**0**	**+6½**
6 Cumulative fiscal adjustment[4]	—	—	−1	−2	−2
7 Public corporations' market and overseas borrowing	0	+½	0	0	0
8 PSBR	**−1**	**+6**	**+11**	**+12**	**+7**

[1] *Rounded to the nearest £½ billion. There have been no significant classification changes affecting the items in this table since the last FSBR.*
[2] *Using same measurement conventions as Table 2A.4: see footnote 1 to that table. The allocation of tax receipts between North Sea and other is affected by the treatment of advance corporation tax set off.*
[3] *Includes changes in debt interest and other items.*
[4] *Line 6 = lines 8 − 7 − 1 + 5.*

3 The economy: recent developments and prospects to mid-1992

Summary

Inflation

3.01 Retail price inflation has fallen from its peak last autumn. It is set to fall sharply in 1991, to 4 per cent in the fourth quarter, and to $3\frac{3}{4}$ per cent by mid-1992.

Demand and activity

3.02 GDP fell in the second half of 1990, with weakening domestic demand, and is likely to continue to fall in the first half of 1991. Activity should recover in the second half of the year, though in 1991 as a whole GDP is forecast to be 2 per cent lower than in 1990. The recovery is likely to gather pace in 1992.

Labour market

3.03 Unemployment has risen sharply since the autumn, reflecting the weakness of activity. With the prospect of a further fall in activity in the first half of 1991, unemployment may continue rising this year, though at a slower rate than recently.

Current account

3.04 The current account deficit is forecast to halve in 1991 to £6 billion, as imports fall in response to falling domestic demand.

Financial developments

3.05 Sterling entered the Exchange Rate Mechanism (ERM) on 8 October. Since then the sterling index has been within a narrow range around 94. Over the same period interest rates have fallen. Monetary growth fell in the second half of last year, and M0 is well within its target range. The public sector is estimated to have been in broad balance in 1990–91 and a public sector borrowing requirement of £8 billion is forecast for 1991–92, largely as a result of the weakness of activity.

World economy

3.06 The world economy was slowing even before the Gulf crisis and the associated rise in oil prices. Oil prices have now fallen back, and are assumed in this forecast to stay close to recent levels. Growth in the major seven economies is expected to fall to $1\frac{1}{4}$ per cent in 1991, the lowest rate since 1982. With slower growth and lower oil prices, inflation is likely to edge down.

Risk and uncertainties

3.07 Table 3.1 shows average errors from past forecasts. These provide a rough guide to possible margins of error on the new forecasts, and should be borne in mind when interpreting and assessing the forecasts. On this occasion there is added uncertainty about the effects of the Gulf war and its aftermath, and the difficulty of predicting turning points in economic activity.

Table 3.1 Economic prospects: summary

Percentage changes on a year earlier unless otherwise stated

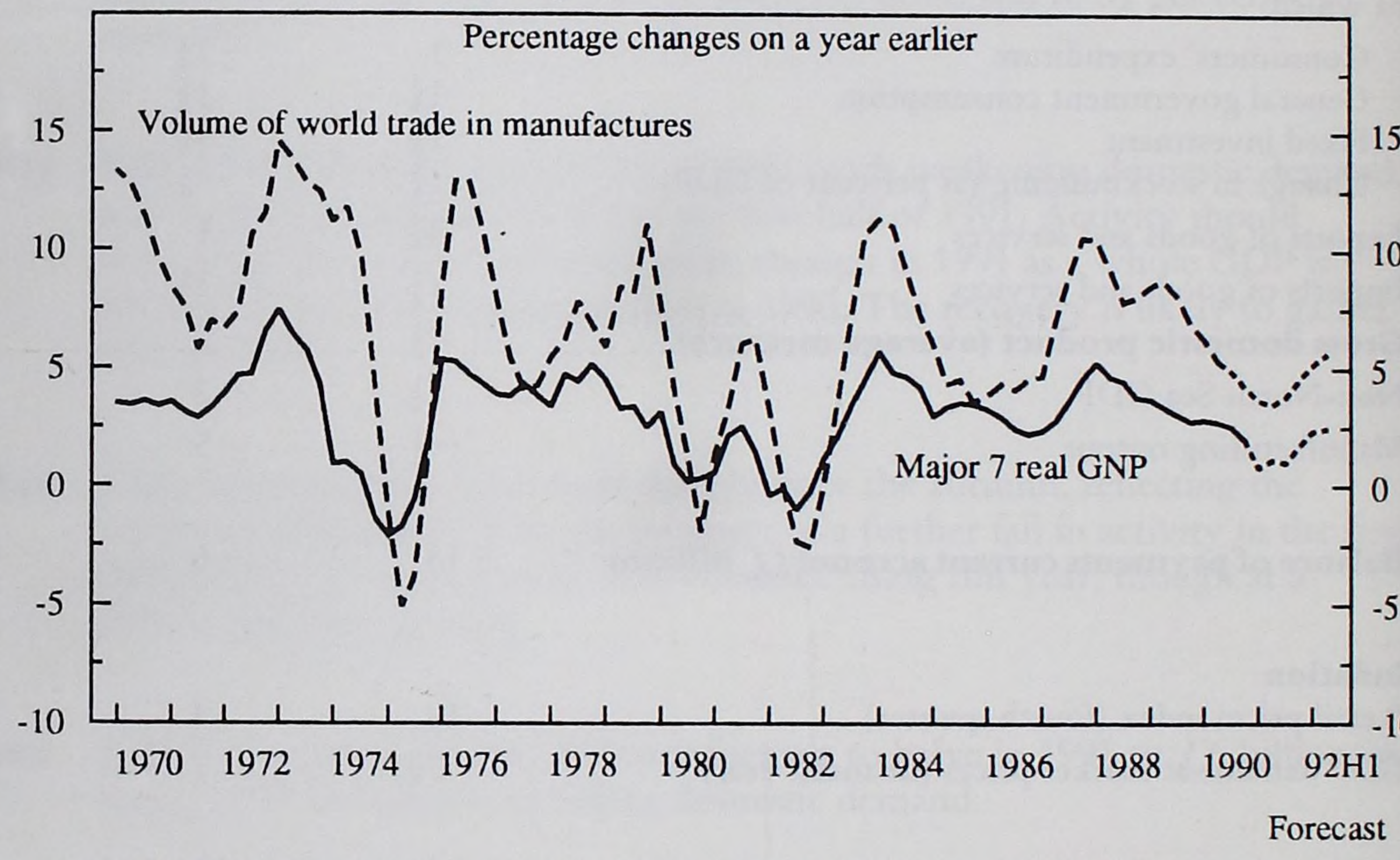
	1990	Forecast 1991	Forecast 1992 H1	Average errors from past forecasts[1]
GDP and domestic demand at constant prices				
Domestic demand of which:	0	$-2\frac{3}{4}$	$2\frac{1}{4}$	1
Consumers' expenditure	1	$-1\frac{3}{4}$	$2\frac{1}{4}$	$1\frac{1}{4}$
General government consumption	$1\frac{3}{4}$	$1\frac{1}{2}$	$1\frac{1}{4}$	1
Fixed investment	$-1\frac{3}{4}$	$-9\frac{3}{4}$	$1\frac{1}{4}$	3
Change in stockbuilding (as per cent of GDP)	$-\frac{3}{4}$	$-\frac{1}{4}$	$\frac{1}{2}$	$\frac{1}{2}$
Exports of goods and services	$4\frac{3}{4}$	1	$4\frac{3}{4}$	$1\frac{3}{4}$
Imports of goods and services	$1\frac{1}{2}$	$-1\frac{1}{2}$	$4\frac{3}{4}$	$2\frac{1}{4}$
Gross domestic product (average measure)	$\frac{1}{2}$	-2	2	1
Non-North Sea GDP	$\frac{1}{2}$	-2	$1\frac{3}{4}$	$\frac{3}{4}$
Manufacturing output	$-\frac{1}{2}$	-5	$2\frac{1}{4}$	$1\frac{1}{4}$
Balance of payments current account (£ billion)	-13	-6	-8[3]	$4\frac{1}{2}$
Inflation				
Retail prices index (fourth quarter)	10	4	$3\frac{3}{4}$[4]	$1\frac{1}{2}$
GDP deflator at market prices (financial year)[2]	$7\frac{3}{4}$	7		$\frac{3}{4}$
Money GDP at market prices (financial year)[2]	$7\frac{1}{4}$	6		$1\frac{1}{2}$
£ billion	547	580		
PSBR (financial year)				
£ billion	$-\frac{3}{4}$	8		$5\frac{3}{4}$
per cent of GDP	$-\frac{1}{4}$	$1\frac{1}{4}$		1

[1] *Average absolute errors over the previous ten years.*
[2] *Estimates of money GDP and the GDP deflator for periods before the second quarter of 1990 have been adjusted to remove the discontinuity arising from the abolition of domestic rates.*
[3] *At an annual rate.*
[4] *Q2 on Q2.*

World economy

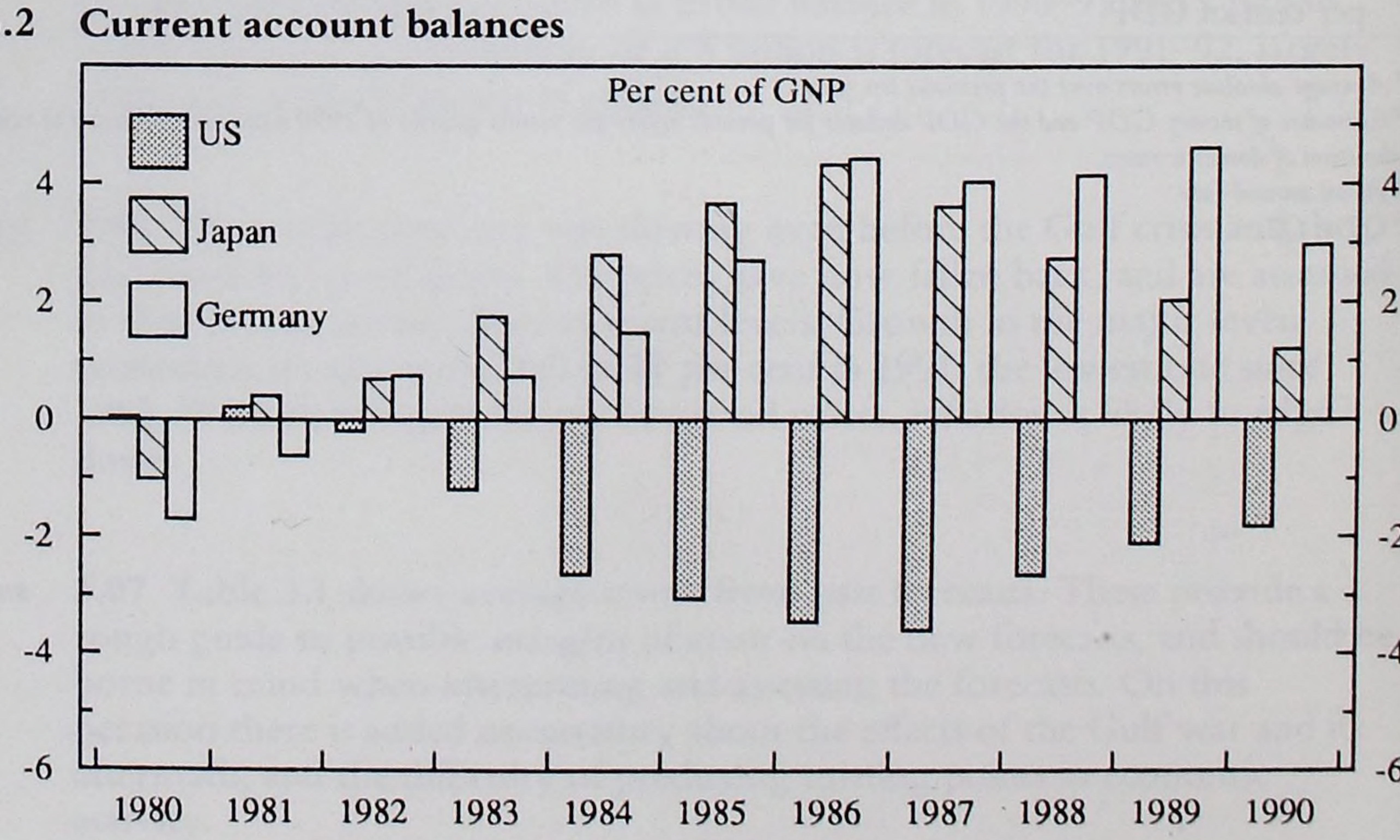
Recent developments **3.08** After several years of buoyant activity, the growth rate of the major seven economies slowed in 1990. Although growth remained strong in Japan and Germany, output was falling towards the end of the year in the US, Canada and France, as well as in the UK. In Japan and Germany there are now tentative indications of slower growth. The growth of world trade in manufactures is estimated to have fallen to about 5 per cent in 1990, its lowest rate since 1986 and well below that of recent years.

Chart 3.1 **World trade and activity**



3.09 Current account surpluses and deficits in the major three countries narrowed significantly in 1990, partly reflecting the relative strengths of activity. The Japanese surplus fell to $1\frac{1}{4}$ per cent of GNP, its lowest since 1982, and in Germany the surplus fell to its lowest level as a proportion of GNP

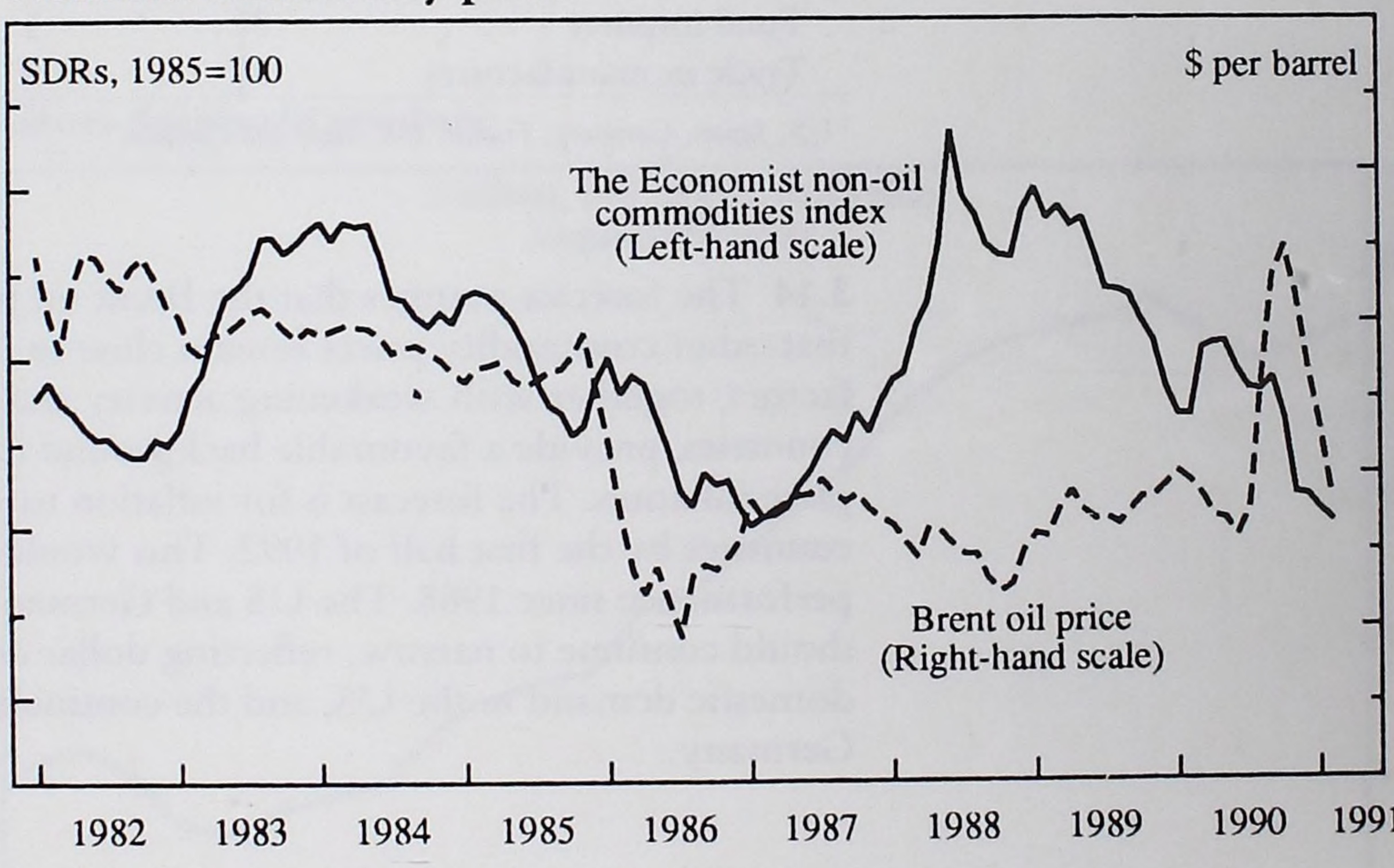
Chart 3.2 **Current account balances**



since 1985. The fall in the US deficit was less than might have otherwise been expected because of a deterioration in the terms of trade in response to the lower dollar.

3.10 Non-oil commodity prices weakened in the second half of 1990; in SDR terms they fell by more than 13 per cent in the year to February 1991. The doubling of oil prices between July and October led to an increase in consumer price inflation in the major seven economies in the same period of about 1 to $1\frac{1}{2}$ percentage points. More recently, the fall in oil prices has helped to ease inflationary pressures. But even excluding oil price effects, inflation has started to decline, especially in those countries where growth has now slowed.

Chart 3.3 Nominal commodity prices



3.11 Since the autumn, US short term interest rates have fallen and German rates have risen. Real interest rates in most of the major European countries rose in 1990, to around 6 to 7 per cent by the end of the year, well above the levels seen for most of the 1980s. In contrast, US real interest rates fell to less than 2 per cent.

Forecast

3.12 The recession in the US is forecast to be quite short-lived and relatively mild. Growth is expected to resume by the second half of this year, helped by an upturn in consumers' expenditure, which has been little changed since late 1989. In France and Italy growth in 1991 is expected to be around $1\frac{1}{2}$ per cent, somewhat slower than in 1990. In Japan and Germany growth is expected to moderate, to about 3 per cent in the second half of the year. For the G7 as a whole the forecast GNP growth of $1\frac{1}{4}$ per cent this year would be the slowest since the 1982 recession. Slower growth of business investment is expected to be a common feature among the G7 countries.

3.13 The recovery in North America, albeit uncertain in its timing and extent, is the main reason why G7 growth is forecast to increase to $2\frac{1}{2}$ per cent in the first half of 1992. Growth of world trade in manufactures follows the path of G7 activity closely, falling to $3\frac{3}{4}$ per cent in 1991 before recovering in the first half of 1992 to a rate a little below the average of the last ten years.

Table 3.2 World economy

	Percentage changes on a year earlier			
		Estimate	Forecasts	
	1989	1990	1991	1992 H1
Major seven countries[1]				
Real GNP	$3\frac{1}{4}$	$2\frac{1}{2}$	$1\frac{1}{4}$	$2\frac{1}{2}$
Domestic demand	3	$2\frac{1}{2}$	1	$2\frac{1}{2}$
Industrial production	$3\frac{1}{2}$	$1\frac{1}{2}$	$\frac{1}{2}$	$2\frac{1}{2}$
Consumer price inflation	$4\frac{1}{2}$	5	$4\frac{1}{2}$	$3\frac{1}{2}$
World trade, at constant prices				
Total imports	$7\frac{1}{2}$	5	$3\frac{1}{4}$	5
Trade in manufactures	$8\frac{1}{2}$	5	$3\frac{3}{4}$	$5\frac{1}{2}$

[1] *US, Japan, Germany, France, UK, Italy and Canada.*

3.14 The forecast assumes that the Brent oil price averages \$18 a barrel and that other commodity prices remain close to their recent low levels. These factors, together with weakening activity and high real interest rates in most countries, provide a favourable background for a reduction in consumer price inflation. The forecast is for inflation to average $3\frac{1}{2}$ per cent in the G7 countries by the first half of 1992. This would be the best inflation performance since 1988. The US and German current account balances should continue to narrow, reflecting dollar depreciation in 1990 and weak domestic demand in the US, and the continuing effects of unification in Germany.

UK demand and output

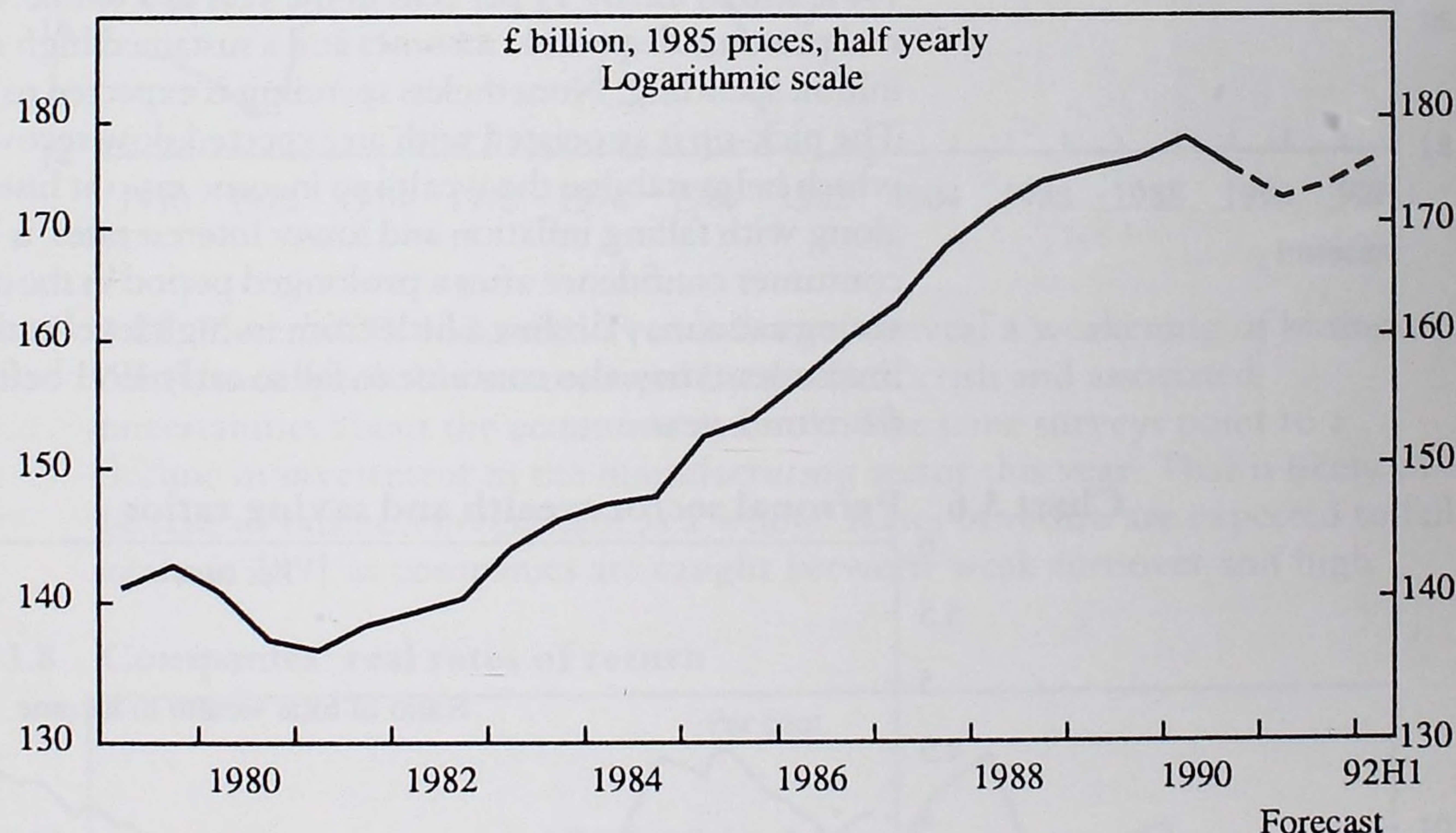
3.15 After signs of seemingly renewed vigour early in 1990, domestic demand fell through the final six months as persons and businesses cut their spending. These developments tipped the economy into recession, with GDP falling $1\frac{3}{4}$ per cent between the first and second halves of 1990. Even so, GDP rose $\frac{1}{2}$ per cent in the year as a whole.

3.16 Domestic demand is forecast to go on falling in the early months of 1991, but at a slower rate than in late 1990. While it is always difficult to predict turning points, a recovery is forecast from around the middle of the year. It could be slow initially, and domestic demand may fall by $2\frac{3}{4}$ per cent in 1991 as a whole. Over the same period GDP is forecast to fall by 2 per cent. The recovery is expected to gather pace next year, with both domestic demand and GDP forecast to rise by over 2 per cent in the year to the first half of 1992.

3.17 The initial source of the recovery is likely to be a revival of consumer confidence in response to falling inflation and lower interest rates. This will stimulate both consumer spending and activity in the housing market. There should also be a contribution from stocks—slower de-stocking in the first instance—but other business spending may not pick up until 1992. Export growth too should begin to pick up later this year with the recovery in the US and other major countries.

3.18 The fall in GDP in the second half of 1990 was spread across most sectors. Manufacturing output, which is usually more cyclical than GDP, fell by 5 per cent between March and December 1990, and by $\frac{1}{2}$ per cent in the year as a whole. Output of the service and construction sectors of the economy, both of which enjoyed very rapid growth during the late 1980s, fell by nearly 1 per cent in the second half of last year. Manufacturing output is expected to fall by 5 per cent in 1991, though growth is projected to pick up during the year, and into 1992.

Chart 3.4 **Gross domestic product**

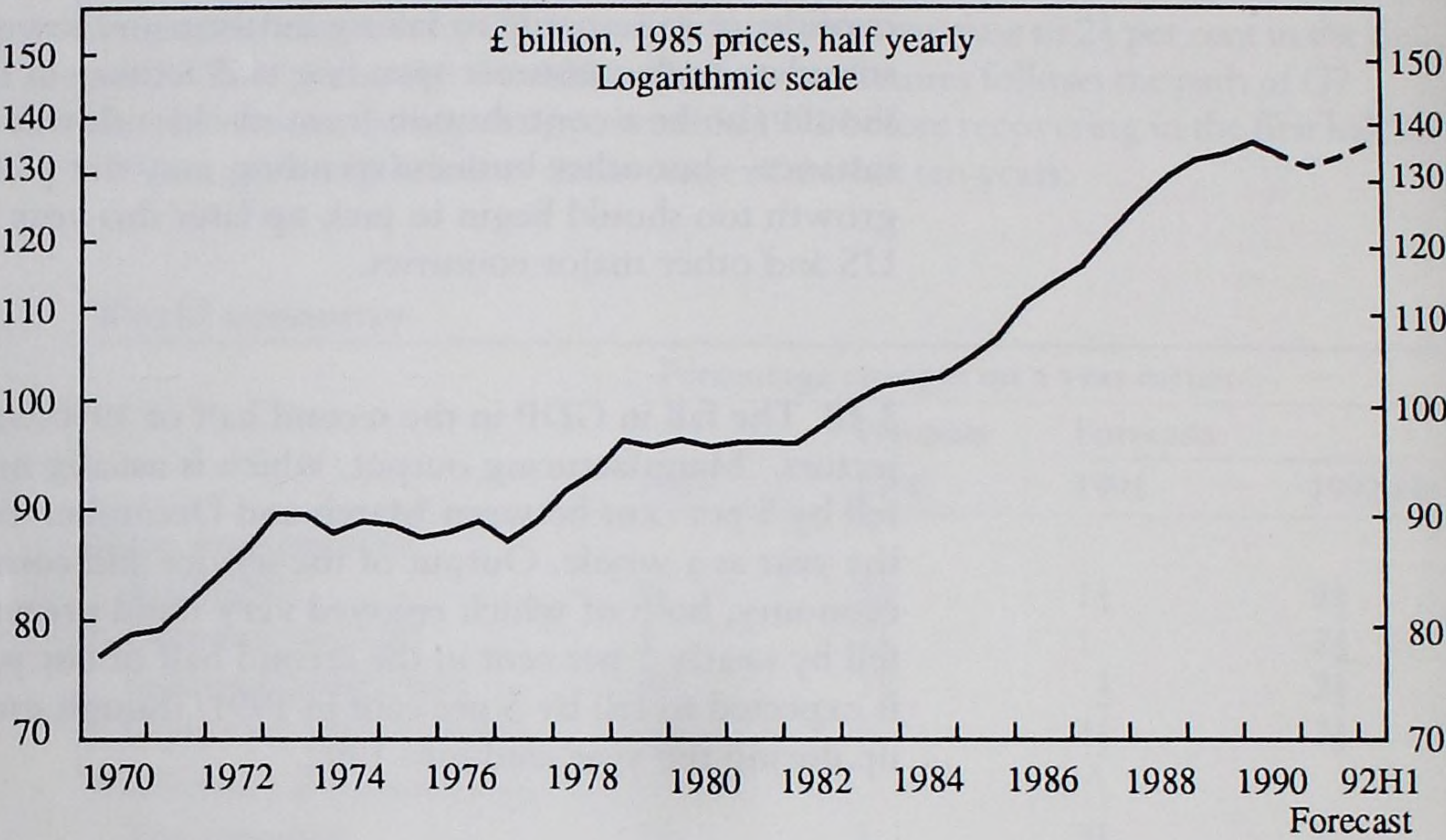


Domestic expenditure

Personal sector

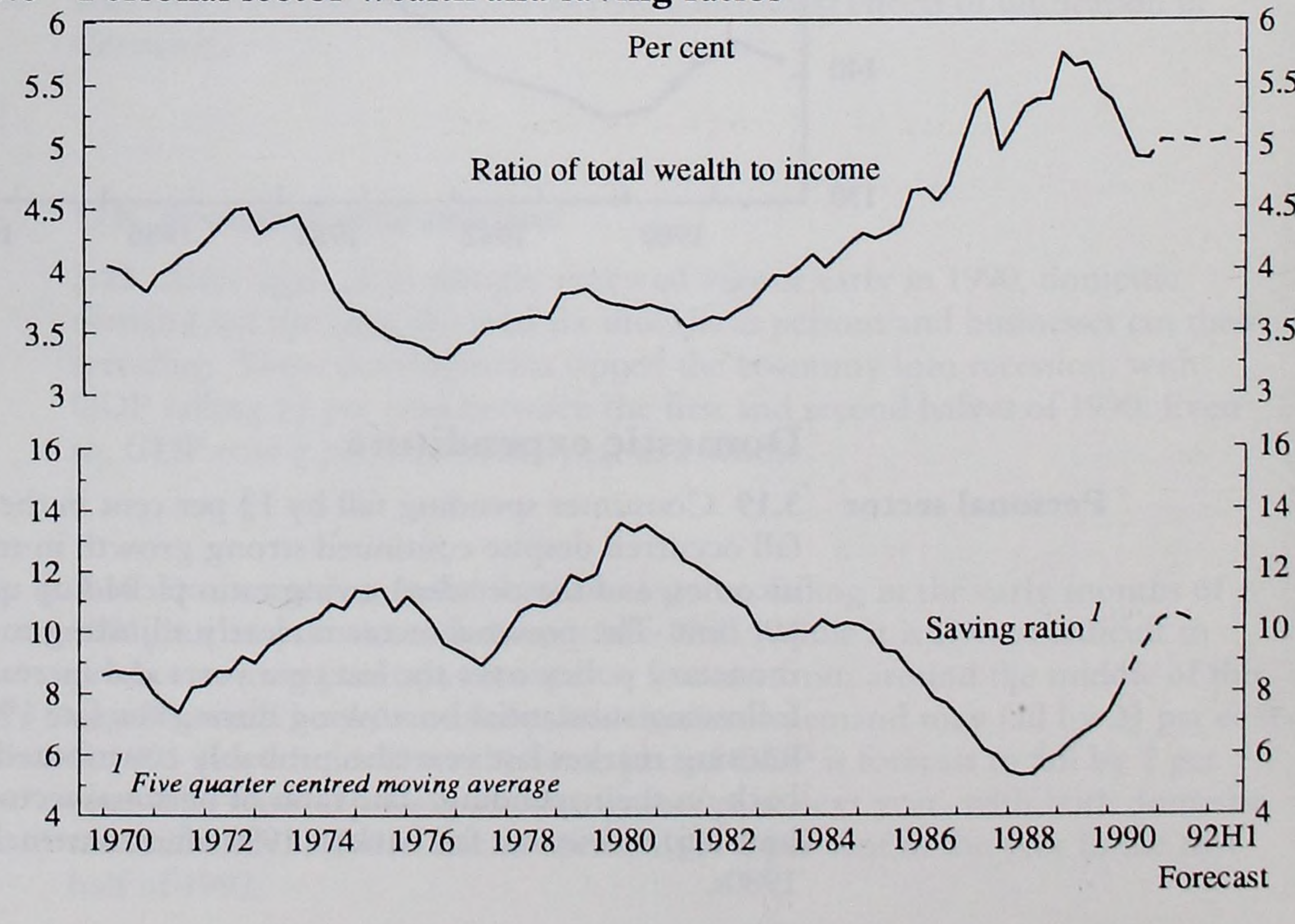
3.19 Consumer spending fell by $1\frac{3}{4}$ per cent in the second half of 1990. The fall occurred despite continued strong growth in real personal disposable incomes, and the personal saving ratio picked up quite sharply to nearly 11 per cent. The personal sector is clearly adjusting to the combination of tight monetary policy over the last two years and increased debt servicing needs following substantial borrowing during the late 1980s. The weakness of the housing market last year also probably contributed to consumers cutting back on their spending. The ratio of personal sector wealth (including housing) to income fell back in 1990 after extremely rapid growth in the late 1980s.

Chart 3.5 Consumers' expenditure



3.20 Consumer spending is projected to go on falling into the early months of 1991, and to fall by $1\frac{3}{4}$ per cent in the year as a whole. Much slower growth in real personal disposable incomes and a sustained high saving ratio are likely to inhibit spending. Nonetheless spending is expected to recover from mid-1991. The pick-up is associated with an expected slow recovery in the housing market, which helps stabilise the wealth to income ratio at historically high levels. This, along with falling inflation and lower interest rates, is likely to regenerate consumer confidence after a prolonged period in the doldrums. The personal saving ratio may decline a little from its high level at the end of 1990. Housing investment may also continue to fall in early 1991 before starting to recover from mid-year.

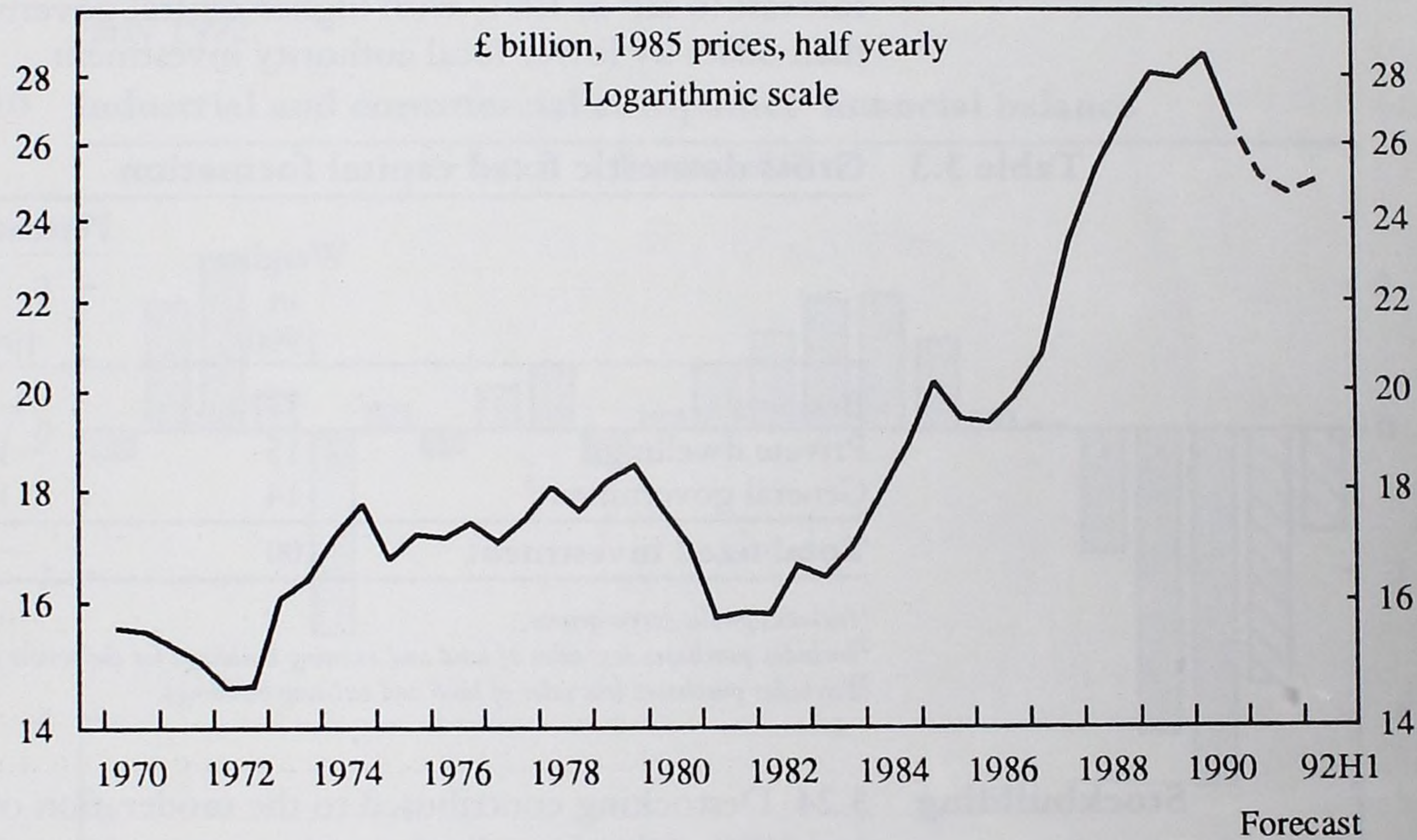
Chart 3.6 Personal sector wealth and saving ratios



Company expenditure and income

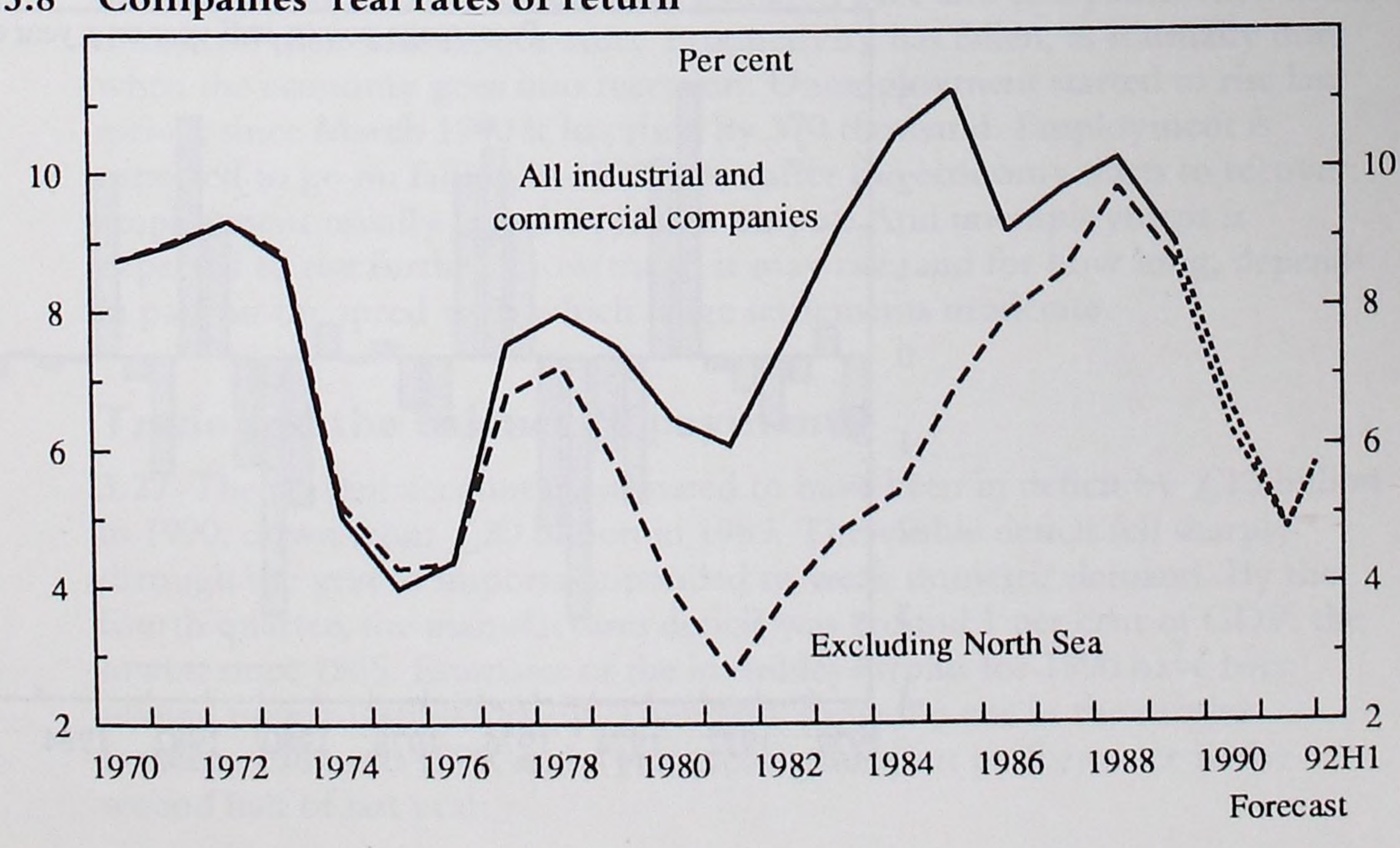
3.21 Business investment rose by a total of 43 per cent in the three years to 1989, prompted by rising real rates of return, rapid growth in output, buoyant business optimism and tightening capacity constraints. After peaking at record levels in early 1990, it fell through the rest of the year as the economy slowed and profitability declined. Companies also faced the need to correct a difficult financial situation, partly induced by their strong borrowing to finance the investment and take-over booms of the late 1980s.

Chart 3.7 Business investment



3.22 Recent CBI Industrial Trends Surveys reveal a weakening of business confidence, probably exacerbated by the Gulf crisis and associated uncertainties about the economic outlook. The same surveys point to a decline in investment in the manufacturing sector this year. That is likely to be true of business investment as a whole. Rates of return are expected to fall again in 1991 as companies are caught between weak turnover and high

Chart 3.8 Companies' real rates of return



unit labour cost growth. Capacity utilisation will also remain low. Business investment is thus expected to fall by nearly 10 per cent in 1991. Even so, it will still be at historically very high levels. It is forecast to rise only slowly in early 1992; it is usual for the recovery in business investment to lag the general cycle in activity. Rates of return should start to recover in 1992, creating the climate for stronger growth in investment later.

Government investment

3.23 General government investment again rose sharply in 1990. It is forecast to fall in 1991, with higher central government investment more than offset by lower local authority investment.

Table 3.3 Gross domestic fixed capital formation

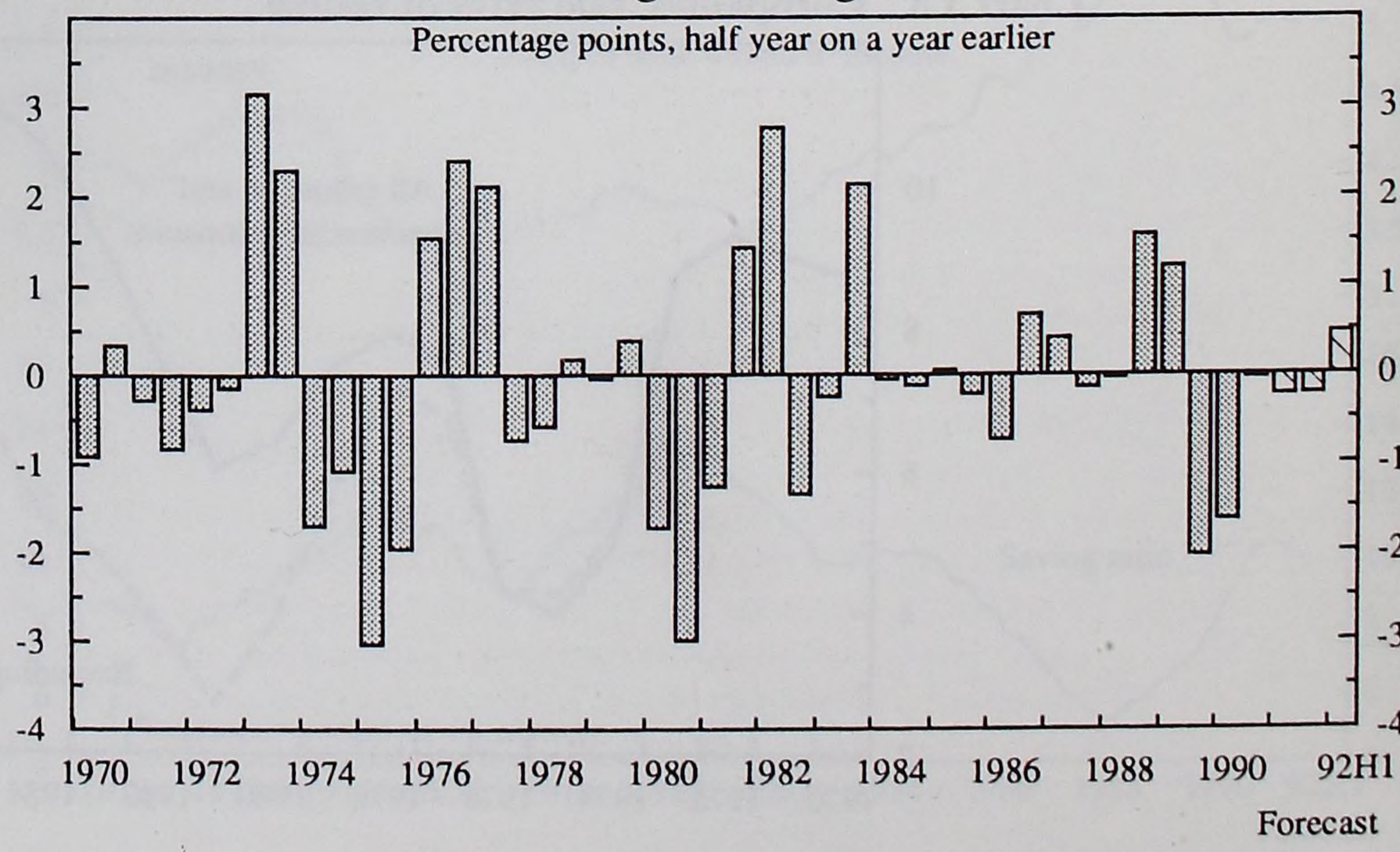
	Weights in 1990	Percentage changes on previous year	
		1990	Forecast 1991
Business[1]	71	$-1\frac{1}{4}$	$-9\frac{3}{4}$
Private dwellings[2]	15	-13	$-11\frac{3}{4}$
General government[3]	14	10	$-6\frac{1}{2}$
Total fixed investment	**100**	$\mathbf{-1\frac{3}{4}}$	$\mathbf{-9\frac{3}{4}}$

[1] *Includes public corporations.*
[2] *Includes purchases less sales of land and existing buildings for the whole economy.*
[3] *Excludes purchases less sales of land and existing buildings.*

Stockbuilding

3.24 Destocking contributed to the moderation of GDP growth in late 1989 and 1990, reflecting adjustment by companies to their difficult financial situation. Destocking may continue throughout 1991 for much the same reason. Nonetheless, stocks are likely to play a much smaller role than in previous recessions, and to contribute less to the subsequent recovery. Firms probably entered the present recession with fewer stocks to disgorge, and may enter the recovery with less need to rebuild them.

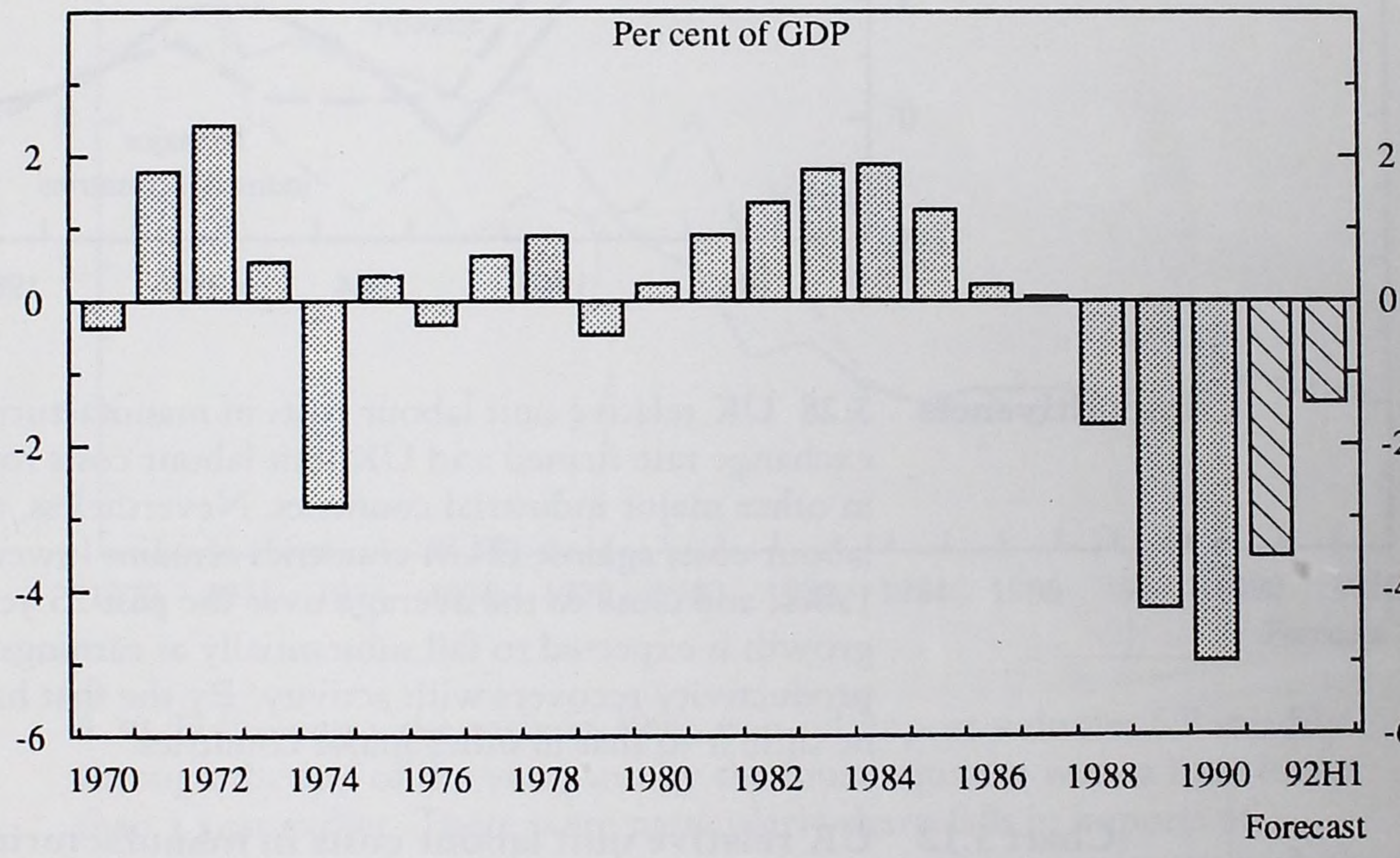
Chart 3.9 Contribution of stockbuilding to GDP growth



Companies' financial position

3.25 Industrial and commercial companies' profits (net of stock appreciation) are estimated to have fallen by $1\frac{1}{2}$ per cent in 1990. Saving also fell, and was insufficient to cover companies' spending on fixed investment and stocks. For the third year running, therefore, companies ran a financial deficit. Profits are likely to remain weak in 1991. Saving, however, is expected to recover as companies face lower tax and interest payments and profits due abroad. Along with reduced spending on fixed investment and stocks, the projected recovery in saving means that the financial deficit should be substantially reduced in 1991, with a further reduction expected in early 1992.

Chart 3.10 Industrial and commercial companies' financial balance



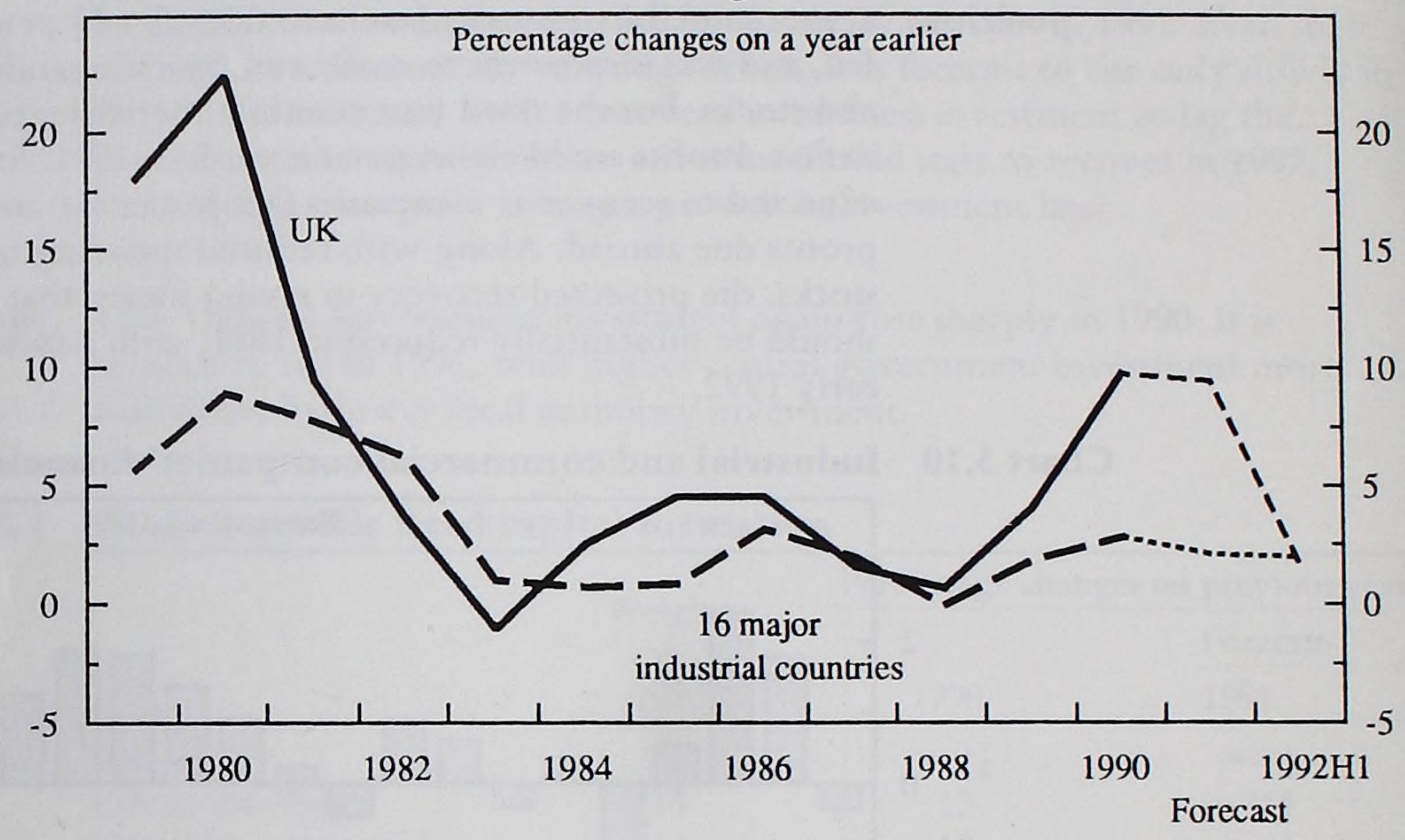
Employment and unemployment

3.26 Latest data from the Department of Employment indicate that employment probably peaked around mid-1990. By then employment had risen by $3\frac{1}{4}$ million since March 1983, on the back of sustained strong growth in activity through most of the 1980s. Employment started to fall in the second half of 1990 as recession gathered pace and companies took action to control their unit labour costs. Productivity has fallen, as it usually does when the economy goes into recession. Unemployment started to rise last spring; since March 1990 it has risen by 370 thousand. Employment is expected to go on falling in 1991, even after the economy starts to recover; employment usually lags the cycle in output. And unemployment is expected to rise further. How much it may rise, and for how long, depends in part on the speed with which wage settlements moderate.

Trade and the balance of payments

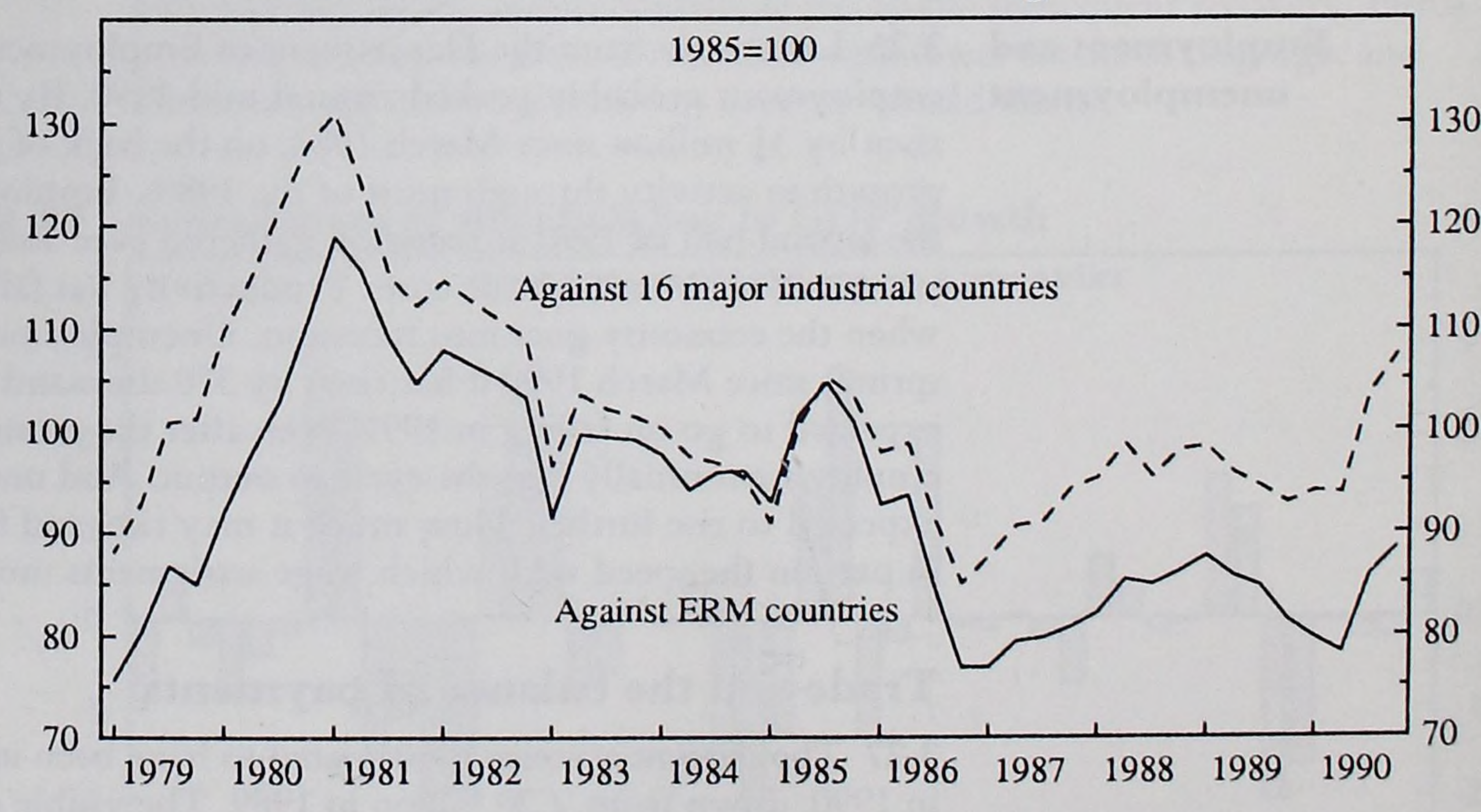
3.27 The current account is estimated to have been in deficit by £13 billion in 1990, down from £20 billion in 1989. The visible deficit fell sharply through the year as imports responded to weak domestic demand. By the fourth quarter, the manufactures deficit was around 1 per cent of GDP, the lowest since 1985. Estimates of the invisibles surplus for 1990 have been revised upwards substantially. They now suggest a rise in the surplus between 1989 and 1990, and a particularly buoyant performance in the second half of last year.

Chart 3.11 Unit labour costs in manufacturing



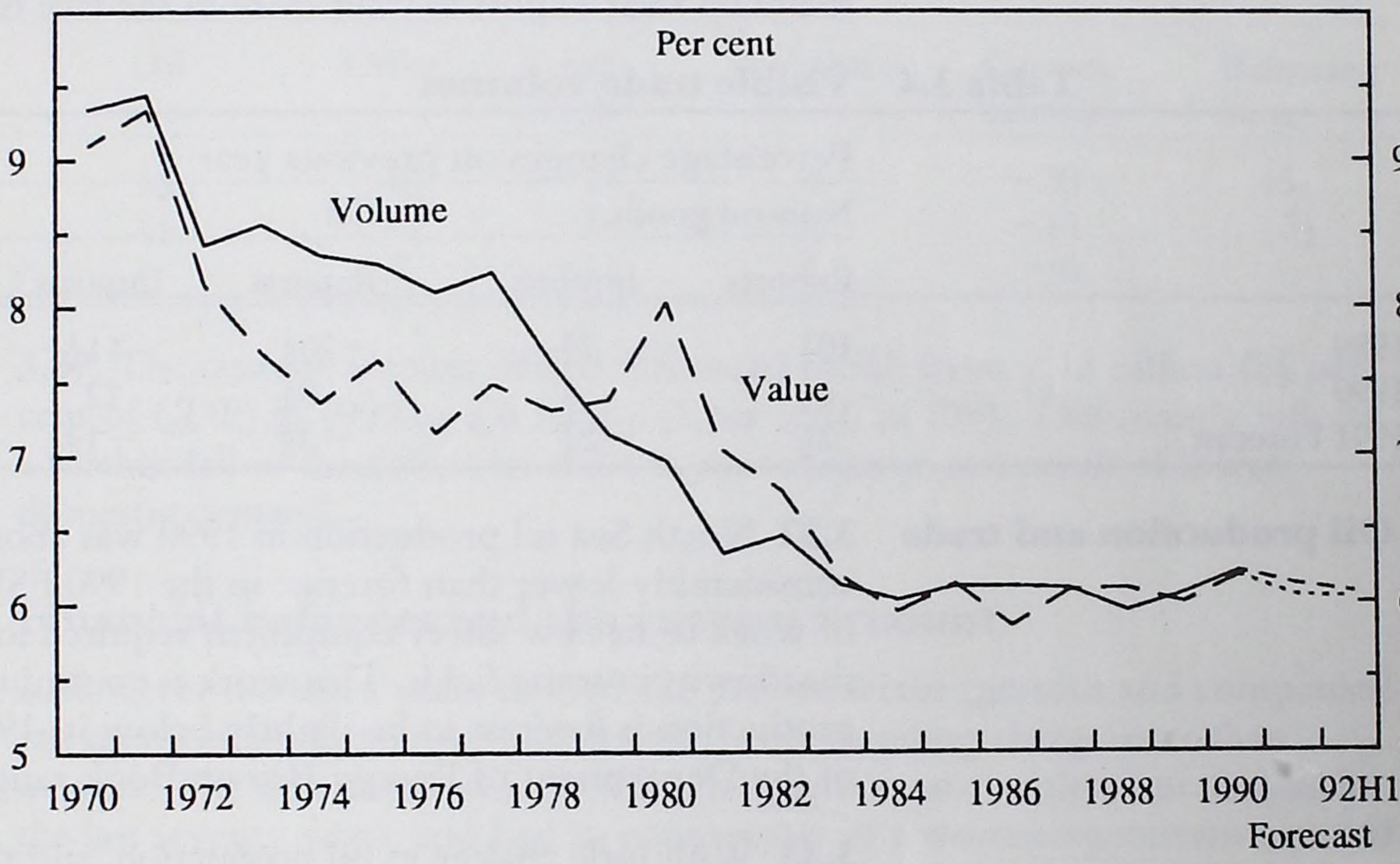
Competitiveness 3.28 UK relative unit labour costs in manufacturing rose during 1990, as the exchange rate firmed and UK unit labour costs rose more rapidly than those in other major industrial countries. Nevertheless, the level of relative unit labour costs against ERM countries remains lower than on average in the 1980s, and close to the average over the past 25 years. UK unit labour cost growth is expected to fall substantially as earnings growth slows and productivity recovers with activity. By the first half of 1992 it is expected to be similar to that in other major countries.

Chart 3.12 UK relative unit labour costs in manufacturing



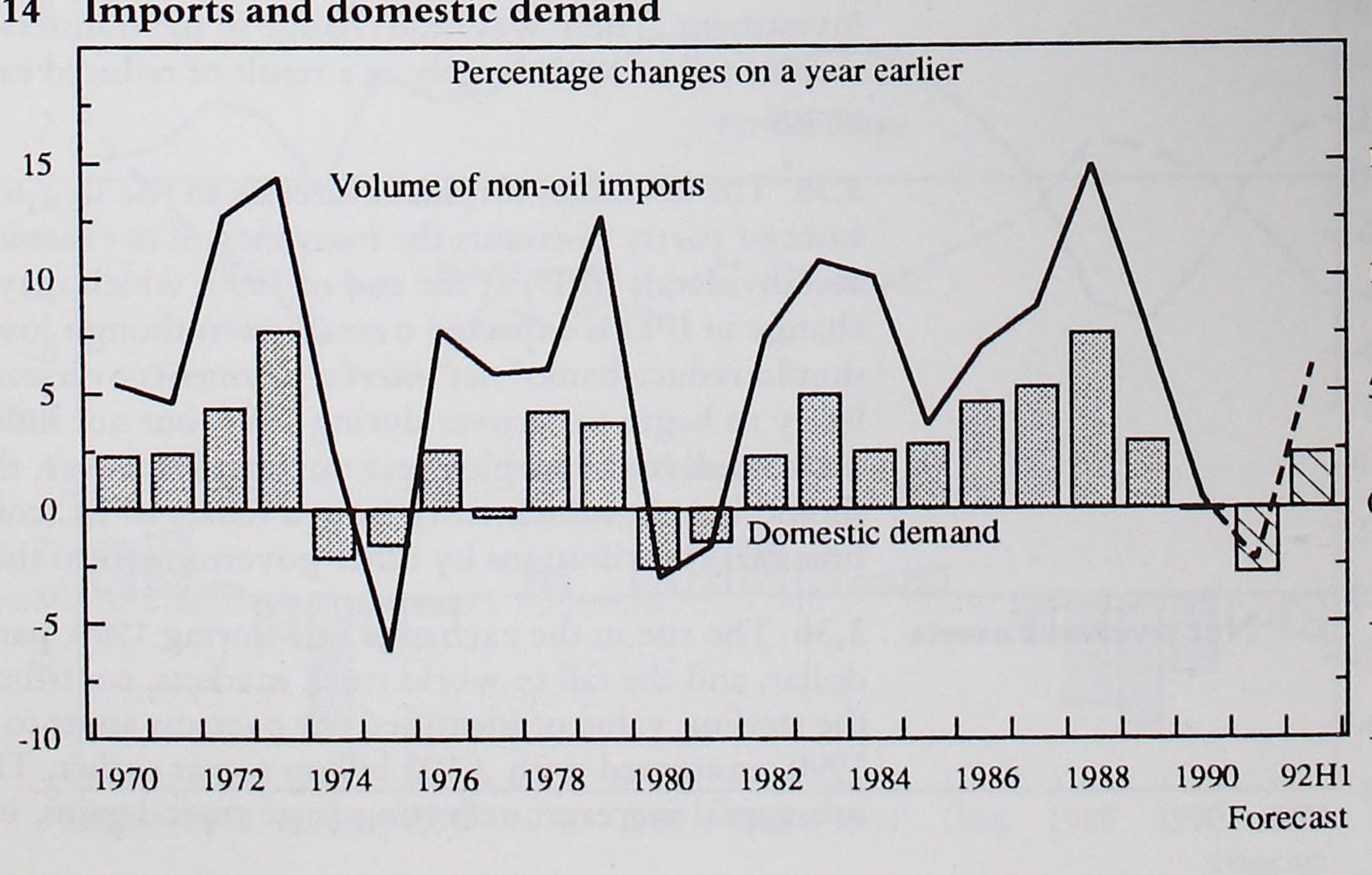
Non-oil trade 3.29 The volume of exports of manufactures rose by $7\frac{3}{4}$ per cent in 1990, following growth of $10\frac{1}{2}$ per cent in 1989, and the UK volume share of world trade in manufactures rose for the second year running. Exports of passenger cars were particularly strong, up 20 per cent in 1990 as a whole. Export growth has, however, eased in recent months as the world economy has slowed. With a further slow-down in world trade in prospect, and the somewhat higher level of the real exchange rate, exports are forecast to grow only slowly in 1991. However, they pick up as world trade growth recovers; by the first half of 1992, the volume of exports of manufactures is forecast to be 4 per cent higher than a year earlier. The UK's share of world trade in manufactures is forecast to be close to the average level of the last three years.

Chart 3.13 UK share of world trade in manufactures



3.30 Following a rise early in 1990, non-oil import volumes fell steadily through the rest of the year, and by the fourth quarter were a little lower than a year earlier. There were particularly sharp falls in imports of passenger cars and capital goods, as consumers and companies cut back their expenditure. Non-oil import volumes are forecast to fall by $2\frac{1}{4}$ per cent in 1991, reflecting the forecast of domestic demand. Import volumes are likely to pick up more rapidly than domestic demand as the economy recovers in

Chart 3.14 Imports and domestic demand



the first half of 1992. This implies a continuation of the historical upward trend in import penetration, which all industrialised economies have experienced, reflecting increasing openness of the world economy.

3.31 Current account adjustment over the past year has also been helped by a rise in the non-oil terms of trade, as sterling import prices fell sharply in response to the firmer exchange rate. Sterling export prices also fell through the year, though by less, as companies reduced export margins to try to maintain their export market share in the face of falling domestic demand.

Table 3.4 Visible trade volumes

	Percentage changes on previous year					
	Non-oil goods		Oil		All goods	
	Exports	Imports	Exports	Imports	Exports	Imports
1989	$10\frac{1}{4}$	$7\frac{3}{4}$	$-20\frac{1}{2}$	$11\frac{3}{4}$	5	8
1990	$6\frac{1}{2}$	$\frac{1}{2}$	$8\frac{1}{4}$	12	$6\frac{3}{4}$	$1\frac{1}{4}$
1991 Forecast	$2\frac{1}{2}$	$-2\frac{1}{4}$	$-3\frac{3}{4}$	$-1\frac{3}{4}$	$1\frac{3}{4}$	$-2\frac{1}{4}$

Oil production and trade

3.32 North Sea oil production in 1990 was about the same as in 1989, but considerably lower than forecast in the 1990 FSBR. The large programme of work to fit new safety equipment required longer than expected shutdowns in some fields. This work is continuing in 1991 and oil production is forecast to be slightly below its 1990 level, close to the centre of the Department of Energy Brown Book range.

3.33 With little change in oil production, and the rise in dollar oil prices in 1990 partly offset by the rise in the dollar-sterling exchange rate, the oil trade surplus in 1990 remained at around £$1\frac{1}{2}$ billion. The sterling oil price is assumed to be lower in 1991 than in 1990 and the oil trade surplus is forecast to decline to £1 billion.

Invisibles

3.34 Following a weak performance in the first half of 1990, the invisibles surplus is estimated to have doubled to £$3\frac{1}{2}$ billion in the second half of the year. In 1990 as a whole the surplus was £5 billion, up £1 billion on the previous year. The rise mainly reflected buoyant net earnings from direct investment. There was little change in the transfers deficit but the services surplus fell in 1990, largely as a result of reduced earnings by the insurance sector.

3.35 The invisibles surplus is forecast to rise to £6 billion in 1991. This forecast partly discounts the buoyancy of net earnings from interest, profits and dividends (IPD) at the end of 1990, which may not be sustained. Little change in IPD is expected overall, even though lower sterling interest rates should reduce banks' net interest payments overseas. The services surplus is likely to begin to recover during 1991, but not sufficiently to prevent a further fall in the surplus year on year. However, the transfers balance should benefit substantially from a rebate of EC contributions and from financial contributions by other governments to the UK's Gulf expenditure.

Net overseas assets

3.36 The rise in the exchange rate during 1990, particularly against the dollar, and the fall in world stock markets, contributed to an estimated fall in the sterling value of identified net overseas assets to £41 billion at the end of 1990, compared with £103 billion a year earlier. This reduction followed substantial increases, reflecting large capital gains, in the previous two years.

The recent revival of the dollar and world stock markets will have partly reversed this fall. The difficulties in measuring certain capital flows (reflected in the balancing item in the overseas account) and in valuing direct investments mean, however, that estimates of net overseas assets are subject to wide margins of error.

Table 3.5 Current account

£ billion

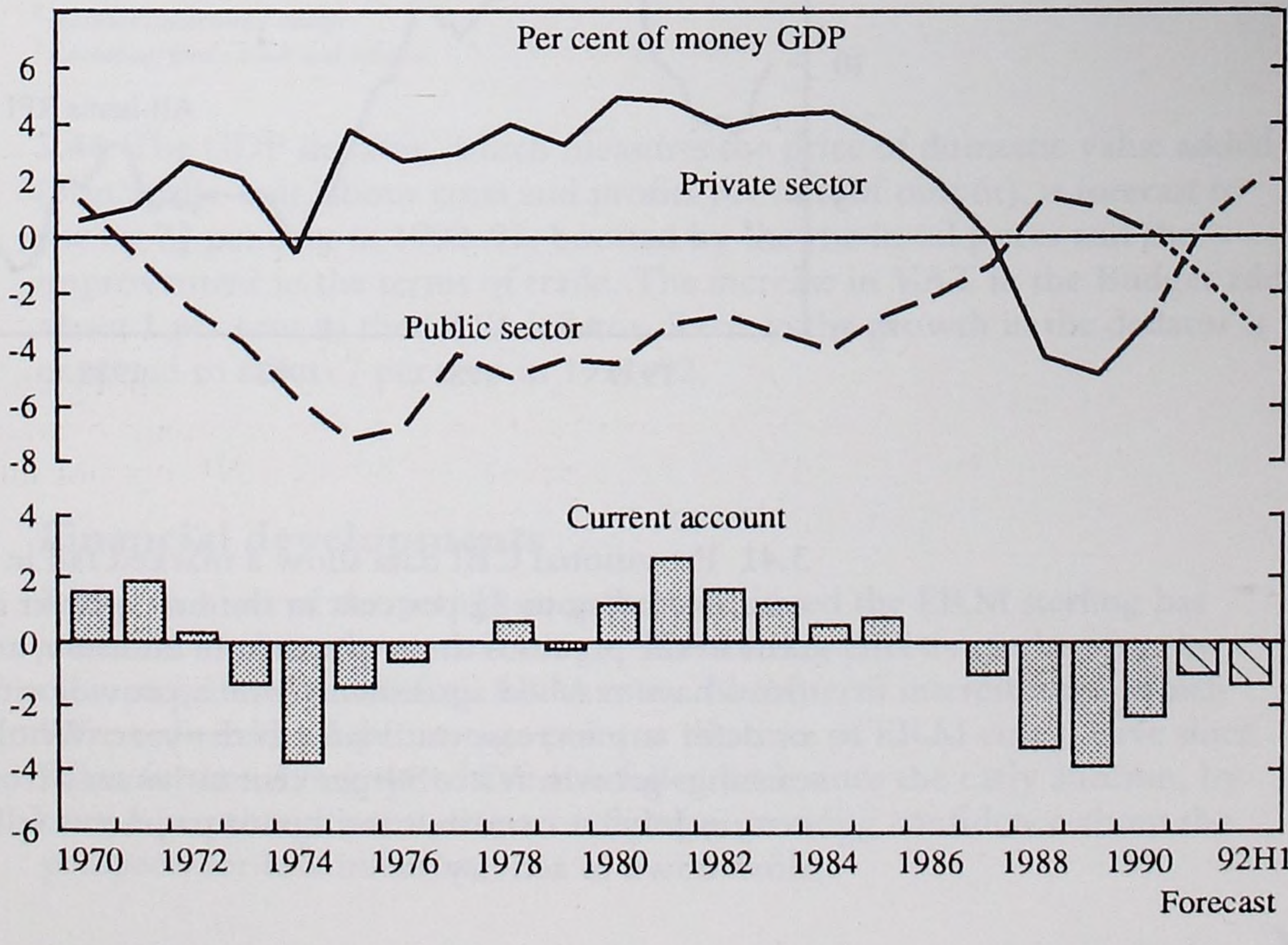
	Manu-factures	Oil	Other	Total visibles	Invisibles	Current balance	Balancing item
1989	−17	$1\frac{1}{2}$	$-8\frac{1}{2}$	−24	4	−20	15
1990	−11	$1\frac{1}{2}$	$-8\frac{1}{2}$	−18	5	−13	$3\frac{1}{2}$
1991 Forecast	−6	1	−7	−12	6	−6	

Current account **3.37** The current account deficit is forecast to fall from £13 billion ($2\frac{1}{4}$ per cent of GDP) in 1990 to £6 billion (1 per cent) in 1991. This mainly reflects a further fall in the deficit on trade in manufactures as a result of lower domestic demand.

Financial balances and the current account

3.38 Over the three years to 1989 the private sector (persons and companies) ran increasingly large financial deficits, with spending rising faster than income. The deterioration in its financial position was without precedent in the last seventy years, and had its counterpart in a worsening current account deficit. With private sector income forecast to rise faster than spending, the private sector financial balance is expected to return to its traditional surplus in 1991 and early 1992. This is reflected in a smaller current account deficit. Within the private sector, both persons and companies are expected to improve their position, with persons increasing their surplus and companies reducing their deficit.

Chart 3.15 Financial balances and the current account

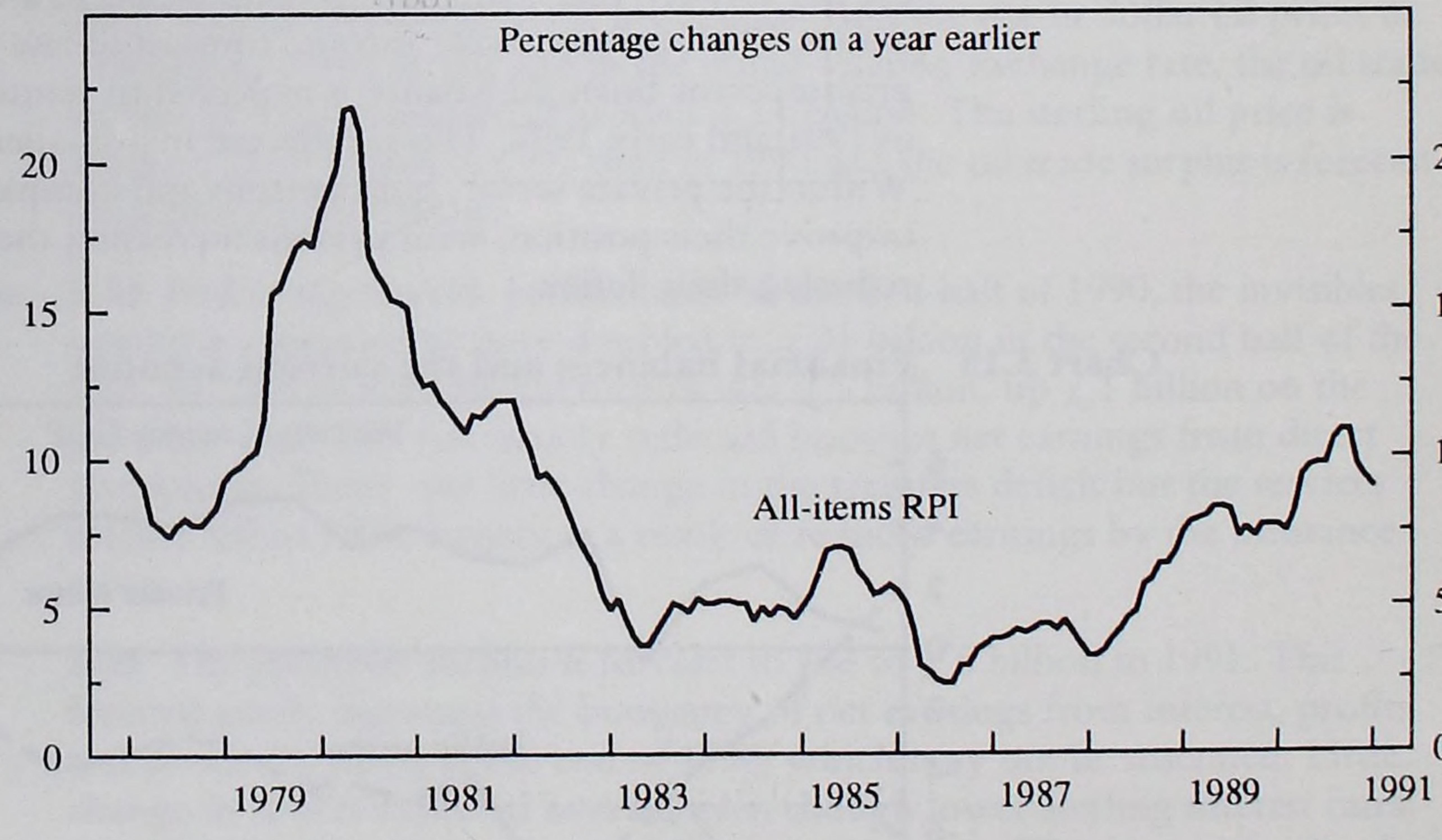


Inflation

3.39 Producer output price inflation (excluding food, drink and tobacco) was $6\frac{3}{4}$ per cent in February, $\frac{1}{2}$ per cent higher than its rate through the summer. This recent pick up in inflation is surprising. It may reflect efforts by producers to defend their profit margins. Margins have been under pressure for some time from the recession and rising costs, especially labour costs.

3.40 Retail price inflation has fallen sharply in recent months, from almost 11 per cent in October to 9 per cent in January. This partly reflects reduced mortgage interest rates in November 1990, and the effects of the mortgage rate rise of November 1989 dropping out of the twelve-month comparison. Petrol prices have also declined as world oil prices have fallen back from their peak in October. But even allowing for these factors, retail price inflation has slowed in response to weak consumer demand and a sharp reduction in food price inflation as supply conditions have improved after the drought of 1989.

Chart 3.16 Retail price inflation



3.41 Provisional CBI data show a marked fall in pay settlements in manufacturing to $8\frac{1}{4}$ per cent in the first quarter of 1991, from around 9 per cent in the previous three quarters. In addition, an increasing number of firms have reached agreements which provide either for no increase in pay or defer any increase until later in the year. Whole economy underlying earnings growth fell to $9\frac{1}{2}$ per cent in January from a peak rate of $10\frac{1}{4}$ per cent in July, as overtime and bonus payments fell in response to the slow-down in activity.

Prospects

3.42 Unit labour cost growth in manufacturing is likely to slow sharply through 1991 and beyond, principally as productivity growth rebounds with the recovery in activity. Earnings growth is also expected to moderate as settlements respond to falling inflation and companies further rein back overtime and bonuses. The CBI's Survey of manufacturers in February suggests that underlying inflationary pressures are abating rapidly. The balance of firms expecting to increase prices in the immediate months ahead was at its lowest ever level. With manufacturing output likely to fall further for a while, the recent pick up in producer output price inflation is unlikely to be maintained. It is expected to fall to 4¾ per cent in the fourth quarter of 1991, declining further to 4 per cent by mid-1992.

3.43 Weak consumer demand will exert strong downward pressure on retail price inflation throughout 1991. Recent cuts in mortgage rates, the mortgage rate rise of March 1990 dropping out of the twelve month comparison, and the net impact of the Budget measures will also contribute to sharply falling inflation. RPI inflation is forecast to be 4 per cent in the fourth quarter of 1991 and 3¾ per cent by the middle of 1992.

Table 3.6 **Retail and producer output price inflation**

	Weights in 1991[1]	Percentage changes on a year earlier 1990Q4	Forecast 1991Q4	Forecast 1992Q2
Food	15	6¾	4¾	3½
Housing[2]	19¼	19½	−6¼	1¾
Other	65¾	8	6¾	4¼
Total RPI	**100**	**10**	**4**	**3¾**
Producer output prices[3]		**6¼**	**4¾**	**4**

[1] *The weights used here are provisional. They are unlikely to differ significantly from the final weights which will be available from the CSO on 22 March.*
[2] *Includes community charge.*
[3] *Excluding food, drink and tobacco.*

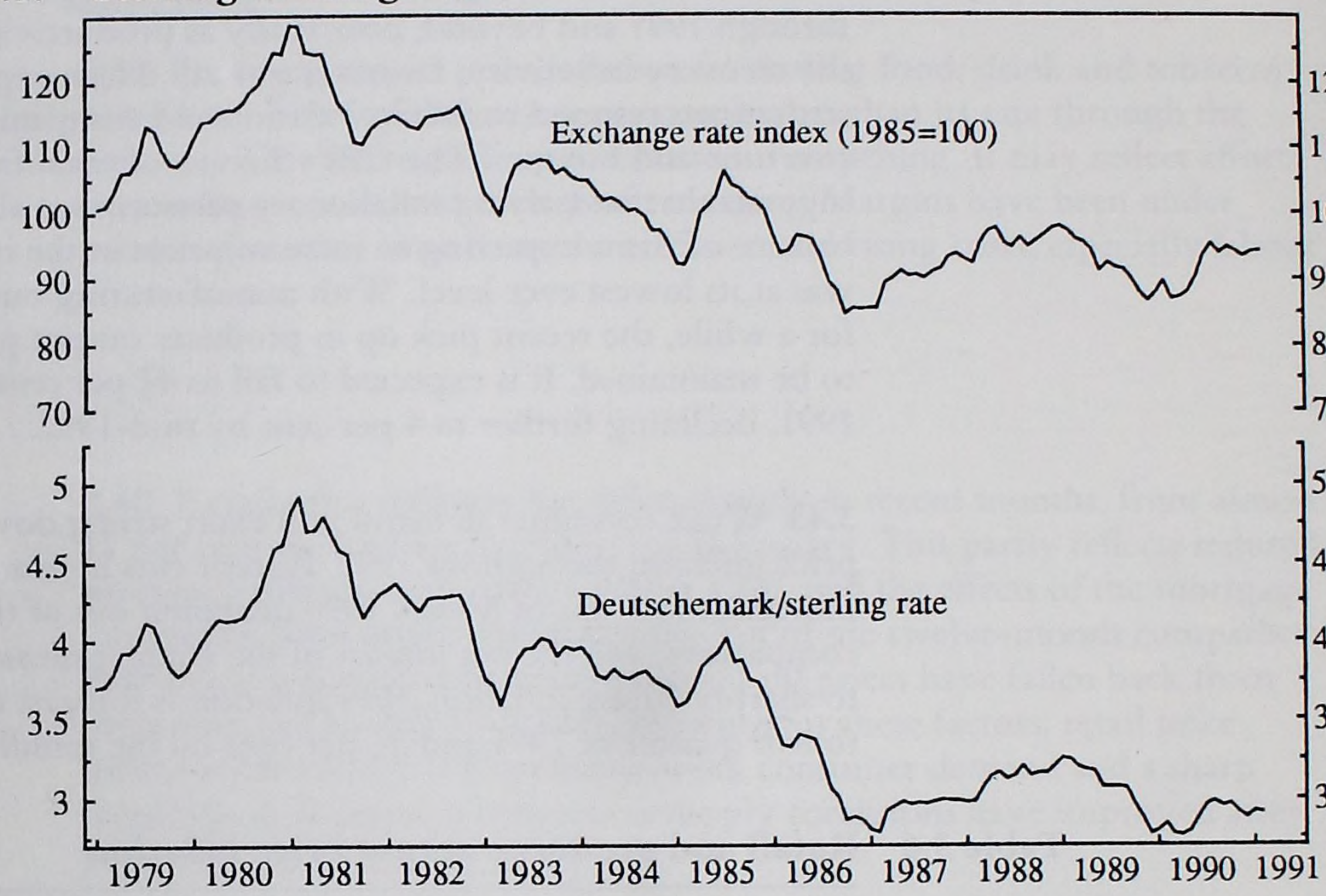
3.44 The GDP deflator, which measures the price of domestic value added (principally unit labour costs and profits per unit of output), is forecast to rise by 7¾ per cent in 1990–91, boosted by the rise in oil prices and the improvement in the terms of trade. The increase in VAT in the Budget adds about 1 per cent to the GDP deflator. Even so the growth in the deflator is expected to fall to 7 per cent in 1991–92.

Financial developments

Exchange rates and interest rates

3.45 For most of the period since the UK joined the ERM sterling has traded in a relatively narrow range. The sterling effective index remains close to its level just before ERM entry. Short term interest rates, which were reduced by 1 percentage point at the time of ERM entry, have since fallen further. Long rates have also fallen back since the early autumn, by over 1 percentage point, in part reflecting growing confidence about the prospects for low inflation.

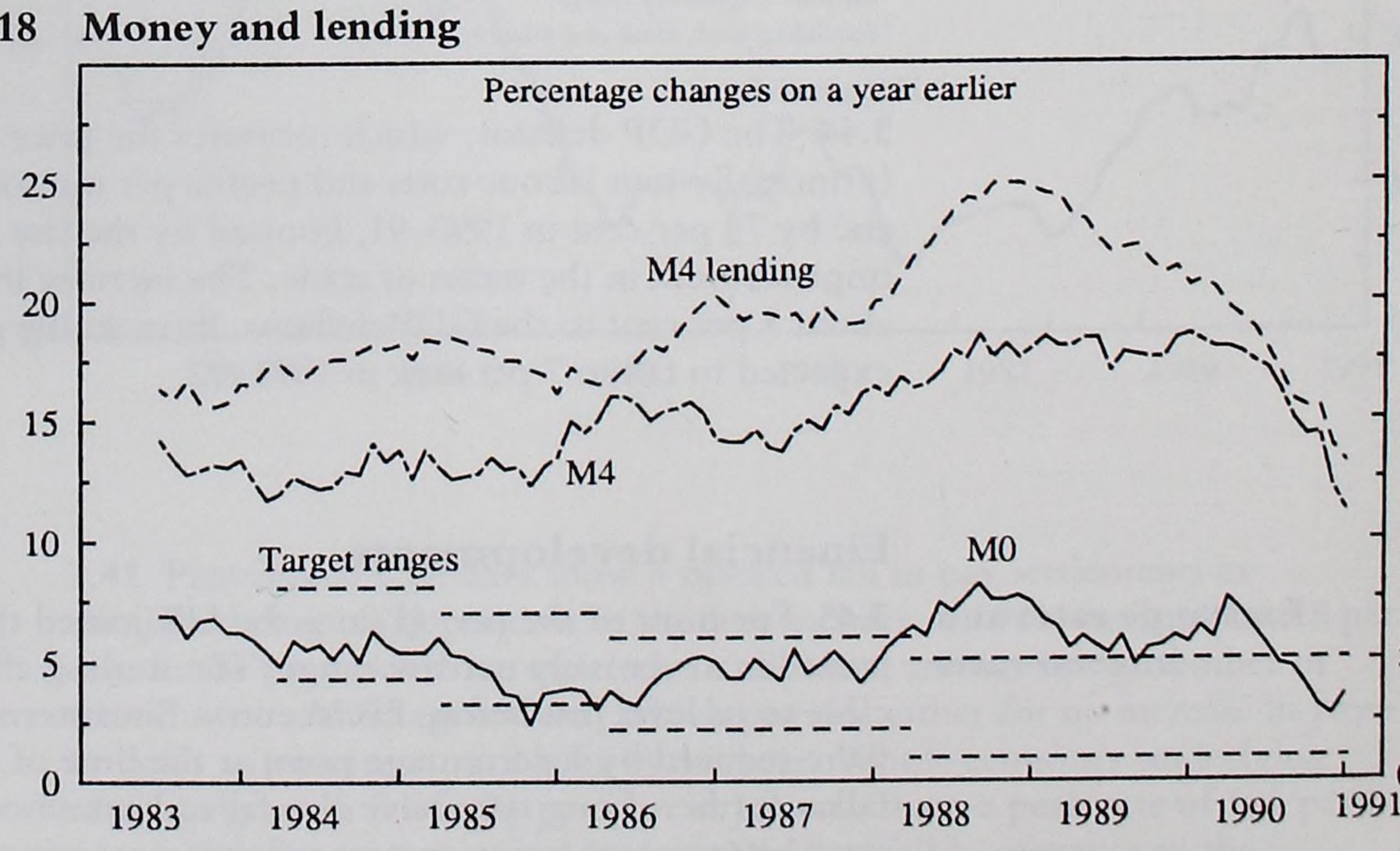
Chart 3.17 Sterling exchange rates



Money and credit

3.46 The year on year growth rate of M0 has fallen from 7½ per cent last spring to around the centre of its target range in early 1991. Broad money growth began to fall in early 1990 from a peak of around 19 per cent. By January the annual growth of M4 was down to 11 per cent. Bank and building society lending had begun to respond to tight monetary policy earlier, as high interest rates reduced lending for house purchase. During 1990 the decline in the growth of credit gathered pace, as industrial and commercial companies also cut back sharply on their borrowing. By the start of 1991 the growth of bank and building society lending was down to 13 per cent, little more than half its peak of two years earlier.

Chart 3.18 Money and lending



Asset prices **3.47** Following strong rises in the second half of the 1980s, asset prices weakened during 1990, reflecting the tightness of monetary policy. There was a substantial fall in the ratio of house prices to average earnings, and real equity prices fell sharply. More recently, however, there have been signs that the housing market may be close to its trough and equity prices have risen strongly since mid-January.

Forecast and outturn

3.48 Table 3.7 compares the main elements of the forecast published in the 1990 FSBR with the outturns for 1990 or the latest estimates for 1990–91.

3.49 Errors on the forecasts of demand, activity and the current account were within, in some cases well within, the average errors from past forecasts. GDP growth was a little less than forecast. Domestic demand was stronger, reflecting unexpected resilience in the first half of the year, but net exports were weaker than forecast. The error on inflation was bigger than average, largely due to a slower than usual response of underlying inflation to the fall in demand, but also because of the effect of the Gulf crisis on petrol prices. The public sector debt repayment is likely to be well below last year's Budget forecast, with large errors on both the income and expenditure sides of the account (see Table 6.2).

Table 3.7 Forecast and outturn

	Percentage changes on a year earlier unless otherwise stated		
	1990 FSBR	Outturn or latest estimate	Average errors from past forecasts
GDP (1990)	1	½	1
Non-North Sea GDP (1990)	¾	½	¾
Domestic demand (1990)	−½	0	1¼
RPI (1990Q4)	7¼	10	1¼
Money GDP (1990–91)[1]	7½	7¼ [2]	1¾
Balance of payments current account (1990, £ billion)	−15	−13	5½
PSBR (1990–91, £ billion)	−7	−¾ [2]	5¼

[1] *Adjusted to remove the discontinuity arising from the abolition of domestic rates.*
[2] *Partly forecast.*

Table 3.8 Gross domestic product and its components

£ billion at 1985 prices, seasonally adjusted

	Consumers' expenditure	General government consumption	Total fixed investment	Change in stocks	Domestic demand	Exports of goods and services	**Total final expenditure**	*Less* imports of goods and services	*Less* adjustment to factor cost	*Plus* statistical adjustment	**GDP at factor cost (average measure)**
1986	231·7	75·2	61·5	0·8	369·1	107·3	476·4	106·0	52·0	−0·6	317·8
1987	243·5	76·2	67·6	1·2	388·5	113·4	501·9	114·3	55·3	−0·6	331·7
1988	260·3	76·7	77·1	3·7	417·8	113·7	531·5	128·9	57·6	0·6	345·6
1989	270·3	77·1	80·2	2·2	429·8	118·8	548·6	138·3	59·3	0·5	351·4
1990	272·9	78·4	78·7	−0·7	429·3	124·5	553·8	140·5	59·8	−0·2	353·3
1991	268·2	79·6	71·1	−1·5	417·4	125·7	543·1	138·3	58·3	0·0	346·5
1989 1st half	134·7	38·1	40·6	2·2	215·6	58·2	273·7	69·4	29·4	0·3	175·2
2nd half	135·6	39·0	39·6	0·1	214·2	60·6	274·9	68·9	29·9	0·2	176·2
1990 1st half	137·6	39·4	40·8	−0·7	217·1	62·8	279·8	71·3	30·3	−0·1	178·2
2nd half	135·3	39·0	37·9	0·0	212·2	61·8	274·0	69·2	29·5	−0·2	175·2
1991 1st half	133·5	39·8	35·6	−1·1	207·8	62·1	269·9	68·3	29·0	0.0	172·6
2nd half	134·7	39·9	35·4	−0·4	209·6	63·6	273·2	70·0	29·3	0·0	173·9
1992 1st half	136·6	40·3	36·1	−0·3	212·6	65·0	277·6	71·6	29·8	0·0	176·2
	Percentage changes on a year earlier[1]										
1989	$3\frac{3}{4}$	$\frac{1}{2}$	4	$-\frac{1}{2}$	3	$4\frac{1}{2}$	$3\frac{1}{4}$	$7\frac{1}{4}$	3	0	$1\frac{3}{4}$
1990	1	$1\frac{3}{4}$	$-1\frac{3}{4}$	$-\frac{3}{4}$	0	$4\frac{3}{4}$	1	$1\frac{1}{2}$	$\frac{3}{4}$	$-\frac{1}{4}$	$\frac{1}{2}$
1991	$-1\frac{3}{4}$	$1\frac{1}{2}$	$-9\frac{3}{4}$	$-\frac{1}{4}$	$-2\frac{3}{4}$	1	−2	$-1\frac{1}{2}$	$-2\frac{1}{2}$	0	−2
1992 1st half	$2\frac{1}{4}$	$1\frac{1}{4}$	$1\frac{1}{4}$	$\frac{1}{2}$	$2\frac{1}{4}$	$4\frac{3}{4}$	$2\frac{3}{4}$	$4\frac{3}{4}$	$2\frac{3}{4}$	0	2

[1] *For stockbuilding and the statistical adjustment, changes are expressed as a percent of GDP.*

4 The Budget measures

4.01 The main tax, national insurance and community charge proposals in the Budget are summarised below. A full list of changes is given in Table 4.1 and they are described in more detail in Annex A. Annex B lists some of the main tax allowances and reliefs, and gives their estimated costs for 1990–91.

Inland Revenue taxes

Income tax

4.02 The personal allowance will be increased in line with the statutory indexation provisions (based on the increase of 9·3 per cent in the Retail Prices Index (RPI) in the year to December 1990). So will the higher rates of the personal allowances and the married couple's allowances for those aged 65 and over. Other allowances will remain at their present levels. The allowances for 1991–92 will be:

personal allowance £3 295 (up £290);

married couple's allowance, additional personal allowance and widow's bereavement allowance £1 720 (no change);

for those aged 65 to 74: personal allowance £4 020 (up £350) and married couple's allowance £2 355 (up £210);

for those aged 75 and over: personal allowance £4 180 (up £360) and married couple's allowance £2 395 (up £210);

income limit for age-related allowances £13 500 (up £1 200).

4.03 The basic rate limit will be increased from £20 700 to £23 700 of taxable income, £1 000 more than under statutory indexation.

Mortgage interest relief

4.04 Tax relief on mortgage interest will be limited to the basic rate of income tax from 6 April 1991.

Benefits-in-kind

4.05 Car benefit scale charges will be increased by 20 per cent from 6 April 1991.

4.06 A standard benefit-in-kind charge for mobile telephones, including those fitted in cars, will be introduced from 6 April 1991.

4.07 The arrangements for setting the "official rate" of interest, which is used to measure the taxable benefit of cheap loans provided by employers, will be revised to bring it more into line with typical mortgage rates.

Training

4.08 Income tax relief for fees paid by trainees for qualifying vocational training courses will be introduced from 6 April 1992.

Employee participation

4.09 The rate of relief for profit-related pay under a registered scheme will be doubled so that all of it will be tax free, subject to the existing limits.

4.10 An incentive will be introduced for employers to set up all-employee share schemes and tax reliefs associated with approved employee share schemes will be extended.

Savings

4.11 The PEP scheme will be extended to allow investment of up to £3 000 a year in a single company Personal Equity Plan, over and above the present limit of £6 000 in an ordinary PEP. It will be possible to transfer shares in an all-employee scheme to a single company PEP without incurring capital gains tax. The range of eligible investments in a PEP will be extended to include equities quoted in other EC states.

4.12 The premium limit on all tax-exempt policies issued by friendly societies will be raised from £150 to £200 a year and restrictions on policies for children will be lifted.

Charitable giving

4.13 The upper limits for tax relief for single donations from companies or individuals will be abolished from 19 March 1991.

Foreign earnings

4.14 The foreign earnings deduction will be extended to enable those forced to break off employment in Iraq or Kuwait because of the Gulf crisis to qualify for relief.

4.15 The period seafarers can spend at home while still qualifying for the foreign earnings deduction on overseas earnings will be doubled.

Business taxation

4.16 The main rate of corporation tax for 1990–91 will be reduced from 35 per cent to 34 per cent; and for 1991–92 to 33 per cent.

4.17 Companies will be allowed to carry back trading losses for three years, instead of one year.

4.18 The profits limit for the small companies' corporation tax rate of 25 per cent will be raised from £200 000 to £250 000 for 1991–92 and the limit for marginal relief will be raised from £1 million to £1·25 million.

4.19 Unincorporated traders will be allowed to set trading losses against capital gains from 6 April 1991.

4.20 Employers whose average monthly PAYE/NIC bill is less than £400 will be allowed to pay PAYE/NIC quarterly rather than monthly.

4.21 The turnover limit below which only a simple three-line statement of account is required for business or rental income will be raised for accounts received after 6 April 1992.

Building societies

4.22 Legislation will be introduced to establish that interest and dividends paid by certain building societies in transitional periods on the change to the present system of accounting for composite rate tax in 1986 may be charged to tax at rates in force for 1985–86.

Capital gains tax

4.23 The capital gains tax annual exempt amount for 1991–92 will be increased in line with the statutory indexation provisions from £5 000 to £5 500 in the case of individuals and from £2 500 to £2 750 in the case of most trusts.

4.24 The qualifying age for capital gains tax retirement relief will be reduced from 60 to 55; and the relief will be available for 100 per cent of the first £150 000 (up £25 000) of real gain, and on 50 per cent of the next £450 000 (up £75 000).

4.25 The period after moving out during which a home can be sold without the owner's private residence relief for capital gains tax being affected will be extended from two to three years. The maximum exemption available when a taxpayer lets part of his or her home will be increased from £20 000 to £40 000.

Trusts

4.26 Measures will be introduced to counter avoidance of capital gains tax through non-resident trusts.

Inheritance tax

4.27 The threshold for inheritance tax will be increased in line with the statutory indexation provisions from £128 000 to £140 000 from 6 April 1991.

Stamp duties

4.28 The abolition of the duties on securities, announced in the last Budget, is now assumed to take place from 1 April 1992, rather than 1 January 1992 as assumed in the Financial Statement and Budget Report 1990–91. Stamp duties on transfers of property other than land and buildings will be abolished from the same day as the duties on securities. Stamp duty on Northern Ireland bank notes will be abolished from 1 January 1992.

Customs and Excise taxes

Value added tax

4.29 The standard rate of value added tax (VAT) will be raised from 15 per cent to $17\frac{1}{2}$ per cent from 1 April 1991.

4.30 The turnover limit for VAT registration will be raised from £25 400 to £35 000 from 20 March 1991.

4.31 The waiting period for relief on written-off bad debts will be reduced from two years to one year from 1 April 1991.

4.32 The rate of serious misdeclaration penalty will be temporarily reduced from 30 to 20 per cent from 20 March 1991 pending the outcome of a review of the penalty. Administrative changes will be made so that the penalty operates more fairly.

4.33 From 1 April 1991, VAT relief for charities will be extended to television, radio and cinema advertising; the sale of donated goods by all charities; one-off fund-raising events by charities' trading subsidiaries; donated medical and scientific equipment used in veterinary research; and certain donated equipment directly used in veterinary research.

Excise duties **4.34** The rate of pool betting duty will be reduced from 40 per cent to $37\frac{1}{2}$ per cent, for a period of four years, provided that the pools promoters pass the full amount saved to a new foundation to be used for the benefit of sports and the arts together with a further contribution of twice that amount which they will collect. The cut will be conditional upon satisfactory arrangements being made, including the terms and conditions for a trust.

4.35 The duty on beer, wines and spirits will rise by 9·3 per cent, in line with the increase in the RPI in the year to December 1990. As already announced, the duty on beer will be levied on the finished product, instead of the " worts ", from a date to be announced.

4.36 The duty on cigarettes, cigars, hand-rolling tobacco and pipe tobacco will rise by 15 per cent.

4.37 The duty on leaded petrol, unleaded petrol and derv will rise by 15 per cent.

Vehicle excise duties **4.38** Duty on cars, buses, light vans, lorries and most other vehicles will remain unchanged. Consequently, the overall increase in motoring duties (fuel duties and vehicle excise duties) will be 11·4 per cent.

National insurance contributions

Benefits-in-kind **4.39** Employers will pay contributions on the benefit of cars provided for the private use of employees from 1991–92, based on the scale charges set for income tax. Employees will be exempted from contributions.

4.40 Employers' current liability to contributions on free fuel available for employees' private use in company cars will be assessed from 1991–92 using the scale charges set for income tax. Employees will be exempted from contributions. Changes to national insurance contributions will be included in a separate Bill to be presented to Parliament.

Community charge

4.41 The community charge throughout Great Britain will be reduced by £140 in 1991–92. The details are set out in the box opposite.

Community charge reduction

The Government's review of local government has concluded that the level of the community charge is unsustainably high, and that the immediate priority is to reduce it. It is therefore proposed to reduce the charge substantially from 1991–92.

The headline community charge for 1991–92 will be reduced throughout Great Britain by £140. The average headline charge will fall from £385 to £245 and the average amount actually paid, after taking account of rebates and reliefs, to below £175. Domestic rates in Northern Ireland will also be reduced. The yield of the community charge and Northern Ireland rates, net of reliefs and rebates, will be reduced by some £4·3 billion in 1991–92 and £4·5 billion in 1992–93, as set out in Table 4.1.

The Government proposes to take powers to pay extra grant to local authorities, and to ensure that this is fully reflected in reduced community charges. This will raise the public expenditure planning total, but there will be an offsetting reduction in local authority self-financed expenditure so that total general government expenditure will be unaffected. The public expenditure consequences are explained in detail in Chapter 5.

The reduction in the community charge will be financed by an increase in central government taxation. The main source of additional revenue proposed in the Budget is an increase in the standard rate of VAT from 15 per cent to $17\frac{1}{2}$ per cent from 1 April.

Table 4.1 Direct effects of Budget measures

See Annex A paragraph numbers	£ million Estimated effect on receipts in: 1991–92 Changes from a non-indexed base	1991–92 Changes from an indexed base	1992–93 Changes from an indexed base
INLAND REVENUE			
Income tax			
1 Increase in personal allowance of £290	−1 420	—	—
2 No change in married couple's allowance (for those aged under 65), additional personal allowance and widow's bereavement allowance	—	+360	+490
3 Increases for those aged 65 to 74 of £350 in personal allowance and £210 in married couple's allowance	−140	—	—
4 Increases for those aged 75 and over of £360 in personal allowance and £210 in married couple's allowance	−60	—	—
5 Increase in income limit for age-related allowances of £1 200	−15	—	—
6 Increase in basic rate limit of £3 000	−470	−140	−240
7 Restriction of mortgage interest relief to basic rate	+220	+220	+420
8 Mortgage interest relief: caravans	*	*	*
9 Benefits in kind: increase in car scales of 20 per cent	+190	+190	+250
10 Benefits in kind: standard charge for mobile telephones	+10	+10	+65
11 Benefits in kind: revised arrangements for beneficial loans	−5	−5	−10
12 Relief for vocational training fees	—	—	−15
13 Full relief for profit-related pay	−35	−35	−60
14 Linkage between approved discretionary and all-employee share schemes	*	*	−15
15 Increase in approved all-employee share scheme limits	*	*	*
16 Foreign earnings deduction: extension for employees in Kuwait or Iraq	−5	−5	—
17 Foreign earnings deduction: extension for seafarers	−10	−10	−10
18 Quarterly payments for small employers (PAYE)	−120	−120	*
19 Increase in turnover limit for simplified accounts	—	—	*
20 Building societies: 1986 transitional provisions	+250	+250	—
21 Abolition of CRT: penalties for false registration for gross payment	*	*	*
Income tax and corporation tax			
22 Life assurance companies	*	*	+20
23 Friendly societies	*	*	*
24 Abolition of upper limit on relief for single donations to charities	*	*	*
25 Relief for gifts of equipment to educational establishments	*	*	*
26 Capital allowances for VAT adjustments on capital goods	*	*	*
27 Capital allowances for toll roads	*	*	*
28 Investment managers: changes to rules	*	*	*
29 Options: relaxation of anti-bondwashing rules	—	—	*
30 Interest on new issues of securities	*	*	*
31 Stock lending and manufactured dividends	*	*	*
Income tax and capital gains tax			
32 Improvements to Personal Equity Plans	*	*	−10
33 Set off of trading losses against capital gains	—	—	−35
Income tax, corporation tax and capital gains tax			
34 Building societies' permanent interest bearing shares	*	*	*

* = *Negligible* — = *Nil*

Table 4.1 Direct effects of Budget measures—*continued*

See Annex A paragraph numbers	£ million Estimated effect on receipts in: 1991–92 Changes from a non-indexed base	 Changes from an indexed base	 1992–93 Changes from an indexed base
Corporation tax			
35 Reduction in main rate for 1990–91 to 34 per cent	−380	−380	−480
36 Reduction in main rate for 1991–92 to 33 per cent	⋆	⋆	−350
37 Extension of carry back for trading losses	⋆	⋆	−250
38 Increase in profits limits for small companies' rate and marginal relief	⋆	⋆	−20
39 Extension of definition of normal commercial loan	⋆	⋆	⋆
40 Increase in limits for provident benefits paid by trade unions	⋆	⋆	⋆
41 Relief for costs of introducing employee share schemes	⋆	⋆	⋆
Capital gains tax			
42 Indexation of the annual exempt amount	—	—	—
43 Improvement of retirement relief	⋆	⋆	−45
44 Extension of private residence relief	⋆	⋆	⋆
Capital gains tax and corporation tax			
45 Non-resident trusts: anti-avoidance measures	⋆	⋆	+10
46 Rebasing of capital gains: technical issues	⋆	⋆	⋆
47 Convertible bonds: changes to exempt status rules	⋆	⋆	⋆
48 Business start-up scheme shares	⋆	⋆	⋆
49 Unremittable gains: technical changes	—	—	—
Oil taxation			
50 Oil field abandonment	⋆	⋆	⋆
51 Proceedings for PRT penalties	⋆	⋆	⋆
Inheritance tax			
52 Indexation of threshold	−45	—	—
Stamp duties			
53 Postponement of abolition of duties on securities	+165	+165	+60
54 Abolition of minor duties	—	—	−15
TOTAL INLAND REVENUE	**−1 870**	**+500**	**−240**
CUSTOMS AND EXCISE			
Value added tax			
55 Increase in standard rate to $17\frac{1}{2}$ per cent	+3 900	+3 900	+5 515
56 Increase in registration limit	−25	−25	−40
57 Revised bad debt relief provisions	−190	−190	−50
58 Revision of VAT penalty regime	−30	−30	−30
59 Minor business measures	⋆	⋆	⋆
60 Reliefs for charities	−5	−5	−5
61 Extension of group treatment	⋆	⋆	⋆
62 Road fuel for business journeys	—	—	—
63 Statutory provision for ex-gratia payments	−5	−5	−5
Car tax			
64 Relief for cars where lessor is a charity	⋆	⋆	⋆
65 Relief for cars used for research	⋆	⋆	⋆

⋆ = *Negligible* — = *Nil*

Table 4.1 Direct effects of Budget measures—*continued*

See Annex A paragraph numbers	£ million Estimated effect on receipts in: 1991–92 Changes from a non-indexed base	 Changes from an indexed base	 1992–93 Changes from an indexed base
Excise duties			
66 Increase in duty on cigarettes, cigars, hand-rolling tobacco and pipe tobacco of 15 per cent	+735	+290	+335
67 Increase in duty on leaded petrol of 15 per cent	+665	+260	+265
68 Increase in duty on unleaded petrol of 15 per cent	+470	+180	+230
69 Increase in duty on derv of 15 per cent	+290	+110	+130
70 Increase in duty on rebated oils of 9·3 per cent	+15	—	—
71 Increase in duty on beer of 9·3 per cent	+145	+5	+5
72 Increase in duty on wine and made wine of 9·3 per cent	+55	—	—
73 Increase in duty on spirits of 9·3 per cent	+105	+5	+5
74 Increase in duty on cider and perry of 9·3 per cent	+5	—	—
75 Reduction in rate of pool betting duty to $37\frac{1}{2}$ per cent	−15	−15	−20
76 Restructuring of gaming licence duty	+10	+10	−5
77 Introduction of registered excise dealers and shippers	*	*	*
TOTAL CUSTOMS AND EXCISE	**+6125**	**+4490**	**+6330**
Vehicle excise duty			
78 No change in rates for cars, buses, lorries and other vehicles	—	−270	−280
79 Increase in rates for motorcycles	+5	+5	+5
80 Single increased rate for tricycles	*	*	*
81 Increase in rates for special machines and recovery vehicles	+5	+5	+5
TOTAL VED	**+10**	**−260**	**−270**
National insurance contributions			
82 Employers' contributions on private benefit of company cars	—	—	+550
83 Employers' contributions on free fuel for private use	—	—	+60
84 Quarterly payments for small employers	−90	−90	*
TOTAL NATIONAL INSURANCE CONTRIBUTIONS	**−90**	**−90**	**+610**
TOTAL CENTRAL GOVERNMENT TAXATION AND NATIONAL INSURANCE	**+4175**	**+4640**	**+6430**
Community charge			
85 Charge reduced by £140 in 1991–92	−4345	−4345	−4540
TOTAL GENERAL GOVERNMENT RECEIPTS	**−170**	**+295**	**+1890**

* = *Negligible* — = *Nil*

Annex A to Chapter 4

This annex explains the general approach used in Table 4.1 to estimate the effects on receipts of Budget measures. It also provides more detail on specific measures. Table 4A.1 shows the effects of major measures announced in the 1990 Budget but only due to be implemented in 1991–92.

Explanatory notes to Table 4.1

Table 4.1 gives the direct effects on receipts of changes in taxation, national insurance and the community charge. Estimates are rounded to the nearest £5 million. "Negligible" means less than £3 million. Measures are costed in the order in which they appear in the table.

The direct effect of a tax change is the difference between the yield of tax which would arise on the basis of the rates of tax, allowances, etc prevailing before the Budget (the pre-Budget regime) and the yield after the changes proposed in the Budget (the post-Budget regime). The difference in yield is generally calculated by applying the pre- and post-Budget regimes to the same tax base. This base is the post-Budget base—that is, the levels of income, consumption, profits, etc forecast for future years on the assumption that all the measures proposed in the Budget take effect.

Thus the direct effects are estimated subject to the constraint that, in general, total incomes and total expenditure are fixed at their post-Budget levels. In other words the estimates in the table do not include income effects—that is, effects arising solely from the impact of changes in taxes on disposable income. Nor do they include the effects of changes in the tax base arising from changes in pre-tax incomes, the general level of prices or other macro-economic variables which may result from the proposed tax changes.

Other behavioural effects are taken into account where it is thought that they will have a significant effect on the yield, for example tax changes which alter the allocation of savings between different financial instruments or affect the composition of expenditure. Some change between the pre- and post-Budget tax bases is thus implicitly allowed for in these cases, subject to the overall constraint on total incomes and expenditure outlined above.

For Customs and Excise taxes and duties, all the estimates of yield incorporate the effects of the tax changes on relative prices and associated changes in the pattern of consumers' expenditure. Aggregate income and consumers' expenditure at factor cost are assumed not to change. Examples where behavioural effects are taken into account for Inland Revenue taxes include changes involving the take-up of a new or modified relief and the abolition of stamp duties on securities.

Most of the figures for direct effects shown in Table 4.1 represent the change in the yield of the tax in question. Where appropriate, however, the effects on the yield of other taxes are also incorporated. For example, the direct effect of a change in the excise duties on tobacco incorporates, in addition to the change in the yield from tobacco duties, the change in the yield of VAT and other excise duties resulting from changes in the composition of consumers' expenditure. As a general rule, only repercussions on the yield of other taxes of the same type are allowed for, such as other taxes on expenditure in the case of tobacco duties but not taxes on income or profits.

The post-Budget forecast of each tax given in Table 1.2 and Chapter 6 takes account of all the effects of the measures announced in the Budget, and not just the direct effects included in Table 4.1.

The figures in the first column of Table 4.1 show the direct effect of the Budget proposals on receipts in 1991–92. Budget proposals are compared with a non-indexed base—that is, with the pre-Budget regime of allowances, thresholds and rates of duty at 1990–91 levels.

The figures in the second column show the direct effect of the Budget proposals on receipts in 1991–92 measured against an indexed base. The indexed base for 1991–92 is obtained by increasing allowances, thresholds and rates of duty in line with the increase in the RPI over the year to December 1990 (9·3 per cent).

The figures in the third column show the direct effect on receipts in 1992–93, also measured against an indexed base. For this comparison, both the Budget proposals and the indexed base for 1991–92 have been further indexed by the forecast movement in the RPI between the fourth quarters of 1990 and 1991 (shown in Table 3.1).

The following paragraphs refer by number to individual line entries in Table 4.1.

Income tax

1 and **3** to **5** The increases in the personal allowance, the age-related personal and married couple's allowances (for those with incomes below the income limit), and the income limit for the age-related allowances are all in line with the statutory indexation provisions (based on the increase of 9·3 per cent in the RPI in the year to December 1990).

2 The married couple's allowance for those aged under 65, the additional personal allowance and the widow's bereavement allowance are all unchanged at £1 720.

6 The increase in the basic rate limit is 14·5 per cent.

7 Higher rate relief for mortgage interest will be withdrawn from 6 April 1991. Higher rate relief for interest on loans for the purchase or improvement of let property is not affected. Transitional higher rate relief on an existing loan will be allowed where relief restricted to the basic rate is also allowable on a second (bridging) loan made before 6 April 1991. Employees paying higher rate tax will be taxed at the difference between basic and higher rates on the benefit of the first £30 000 of beneficial home loans from their employers. The entries in Table 4.1 are calculated on the basis that current mortgage interest rates (assumed to be 13·75 per cent) remain unchanged.

8 Mortgage interest relief will be allowed on a loan for the purchase of a small caravan used or intended to be used as a person's main residence without any requirement for the caravan to be a rateable hereditament.

9 For 1991–92 the scales for taxing car benefits will be increased by 20 per cent from their 1990–91 levels.

10 A new benefit-in-kind charge will be introduced from 6 April 1991 to tax the benefit from the private use of a telephone fitted in a car provided by an employer. Tax will be paid on a standard amount of £200. The same charge will be used to value the private benefit of a mobile telephone, which is already taxable.

11 The arrangements for setting the "official rate" of interest, which is used to calculate the taxable benefit of loans made by employers and the "additional charge" in respect of accommodation provided by employers which costs more than £75 000, will change from 6 April 1991. The present formula (average base rate plus 1·5 per cent) will be discontinued, and the "official rate" will be specified in a Treasury order. The intention is that this will broadly reflect typical mortgage rates. The de minimis limit, under which small benefits from cheap loans (such as those for season tickets) are disregarded, will be increased from £200 to £300 from 1991–92.

12 From 6 April 1992 fees paid by trainees for courses leading to national and Scottish vocational training qualifications up to level 4 will qualify for tax relief. Relief at the basic rate will be given by deduction at source from fees paid; higher rate relief, where applicable, will be given separately. Costs are likely to increase in future years as more qualifying courses become available and with take-up. The cost shown in Table 4.1 excludes an estimated public expenditure cost of £5 million in 1992–93 in respect of relief at source for non-taxpayers.

13 With effect for profit periods starting on or after 1 April 1991, the rate of tax relief for an employee's profit-related pay which is paid under a scheme registered by the Inland Revenue will be doubled to give full tax relief, subject to existing limits. The cost is estimated on the basis that the number of employees in registered schemes will rise by a third in 1992–93.

14 From 1 January 1992 any company participating in both an approved discretionary share option scheme and an approved all-employee scheme (of which the eligible employees have been informed) will be able, in the discretionary scheme, to provide for the grant of options over shares at a price representing a discount of up to 15 per cent of the market value of the shares concerned at the date of grant.

15 The annual limit on the value of shares which may be given to an employee under an approved all-employee profit-sharing scheme will be increased, with effect from 6 April 1991, from the greater of £2 000 or 10 per cent of pay (up to a maximum of £6 000) to the greater of £3 000 or 10 per cent of pay (up to a maximum of £8 000). The limit on monthly savings made by an employee under an approved all-employee savings-related share option scheme will be increased, from a day to be appointed, from £150 to £250.

16 The tax relief for foreign earnings will be extended so that employees in Kuwait and Iraq forced to return to the UK early because of the Gulf crisis, or unable to return to those countries because of it, will be relieved of UK tax on their foreign earnings up to the date of their return to the UK.

17 From 6 April 1991 the limits on the availability of the foreign earnings deduction to seafarers who work abroad for a qualifying period of 365 days will be relaxed. They will lose the deduction only if they return to the UK either for more than 183 days (previously 90 days) or for a period longer than one half (previously one quarter) of the combined time spent overseas and in the UK.

18 For deductions made after 6 April 1991 employers whose average monthly PAYE/NIC bill is less than £400 will be allowed to make payments to the Inland Revenue quarterly rather than monthly. This line shows the effect on income tax receipts. The effect on receipts of national insurance contributions is at line 84 in Table 4.1.

19 Individuals or partnerships who are trading with a total annual turnover of under £10 000, or people with rent from property where gross income is less than £10 000 are able to submit simplified accounts. For accounts received after 6 April 1992 these limits will be increased to a figure to be announced later.

20 Legislation will be introduced to establish that interest and dividends paid by certain building societies on the change to the present system of accounting for composite rate tax in 1986 may be charged to tax at rates in force for 1985–86. This will mean that the Exchequer will not repay amounts collected under the transitional arrangements except to any society which commenced judicial review proceedings before 18 July 1986 challenging the validity of Regulations bringing these payments into charge. The estimate allows for consequential effects on corporation tax.

21 A penalty will be introduced for making a false declaration in order to receive interest from building societies and deposit takers without deduction of basic rate tax.

Income tax and corporation tax

22 A measure will be introduced to give life offices an entitlement within an accounting period to repayments of tax deducted from, and payments of tax credits attaching to, their pension business income. This will give the companies treatment comparable to the self-administered pension schemes. The measure will be linked to the introduction of Pay and File. There will also be changes in the tax rules for general annuity business; and relief as management expenses will be allowed for levies paid under investor protection schemes. The yield in 1992–93 will change to a cost in subsequent years.

23 The limit on premiums payable under tax-exempt life insurance policies with friendly societies will increase from £150 a year to £200 a year. It will be possible to vary existing policies taken out after 31 August 1987 so as to take advantage of the new limit without losing their beneficial tax treatment. The current restrictions on the extent to which friendly societies can write policies for children where the maturity proceeds are free of tax will be removed. These changes will apply to policies written after Royal Assent. From 19 March 1991, societies will also be able to offer small taxable policies to members who already have a tax-exempt policy.

24 The upper limit of £5 million a year or, for non-close companies 3 per cent of dividends, for income tax or corporation tax relief for single donations to charities by individuals or companies will be abolished for donations made on or after 19 March 1991.

25 Relief will be provided for gifts by businesses to educational establishments of equipment which is made, used or sold in the course of the donor's trade.

26 Capital allowances given on computers or buildings will be adjusted where the amount of VAT payable in respect of such assets is retrospectively changed under the VAT capital goods scheme introduced in April 1990.

27 Expenditure on the construction of toll roads will qualify for industrial buildings allowance from 6 April 1991, bringing their treatment into line with other privately financed projects such as toll bridges and tunnels.

28 The rules which exempt UK investment managers acting for non-resident clients will be extended.

29 The anti-bondwashing rules will be relaxed to make it easier to buy or sell shares using options without a tax charge arising.

30 The tax rules governing interest calculated by reference to a period prior to the issue of securities will be amended.

31 Stock lending of overseas securities will be facilitated by removing the limit of three parties in an approved lending chain. In addition, the arrangements for accounting for tax on the manufactured dividends paid by the borrower to the lender will be given firmer statutory backing.

Income tax and capital gains tax

32 With effect from 1 January 1992 it will be possible to subscribe up to £3 000 a year to a Personal Equity Plan (PEP) investing in the shares of a single company, in addition to up to £6 000 (as at present) to an ordinary PEP. It will be possible to transfer shares held in an approved all-employee scheme into a single company PEP without incurring capital gains tax. From late 1991 the range of PEP investments will be extended to equities quoted in other EC states, and to unit and investment trusts with at least half of their holdings in EC equities. And, from 6 April 1991, the limit on investment in unit and investment trusts not meeting the investment requirements will be increased from £900 to £1 500. The cost of these measures is expected to rise in later years.

33 After 5 April 1991, if an unincorporated trader makes a loss which can be set off against his or her other income of the same or the following year, any unused loss can be set against his or her capital gains of those years.

Income tax, corporation tax and capital gains tax

34 Building societies' permanent interest bearing shares that are denominated in sterling will be exempt from tax on capital gains. Interest on these new building society shares will be paid after deduction of income tax.

Corporation tax

35 The rate for 1990–91, which was set in the Finance Act 1990 at 35 per cent, will be reduced to 34 per cent.

36 The rate for 1991–92 will be reduced to 33 per cent.

37 The period for which trading losses can be carried back will be extended from up to one year to up to three years.

38 The profits limit for the small companies' rate of corporation tax of 25 per cent for 1991–92 will be raised from £200 000 to £250 000 and the limit for marginal relief will be raised from £1 million to £1·25 million.

39 A technical change will be made to the definition of a normal commercial loan for group relief and other purposes.

40 The limits for tax exemption for trade unions and employers' associations which pay provident benefits will be raised from £3 000 to £4 000 for gross sums and from £625 to £825 for annuities.

41 Costs incurred by companies on or after 1 April 1991 in establishing approved employee share schemes or statutory employee share ownership plans (ESOPs) will be relieved of tax.

Capital gains tax

42 The capital gains tax annual exempt amount will be increased in line with the statutory indexation provisions (based on the increase of 9·3 per cent in the RPI in the year to December 1990) to £5 500 (£2 750 for most trusts). The estimated full year cost of indexation in respect of 1991–92 liabilities is £10 million.

43 The qualifying age for retirement relief on the disposal of businesses and interests in family companies will be reduced from 60 to 55. The ceiling for the relief will be increased so that, where the full conditions are met, the first £150 000 of gains will be fully exempt and half of any further gains up to £600 000 will be exempt. The present ceilings are £125 000 and £500 000 respectively. The cost of these changes in a full year is £70 million.

44 Three changes will be made to the relief for principal private residences. First, the period after moving out during which a home can be sold without a reduction in the owner's entitlement to this relief will be increased from two to three years. Second, the present exemption, where owners let part or all of their main home, of up to £20 000 of any gains which do not attract the private residence relief will be increased to £40 000. Third, the maximum amount of land which can normally qualify for private residence relief will be changed from one acre to half a hectare.

Capital gains tax and corporation tax

45 A charge to capital gains tax will be made on a trust which ceases to be resident in the UK, and on a settlor who retains an interest in a non-resident trust. The existing rules for charging the gains of non-resident trusts on beneficiaries will be strengthened, and a supplementary charge introduced on payments and benefits which are received. Without these measures there could be a significant loss of tax. The measures themselves may produce a direct yield of £15 million in a full year.

46 The rule in the Finance Act 1988 for rebasing the charge on capital gains to 31 March 1982 includes a provision allowing certain gains deferred between 31 March 1982 and 6 April 1988 to be halved. Technical changes will be made to ensure that the benefit of this relief cannot be given twice in respect of the same gains, and that the value of the relief cannot be increased by the taxpayer making a claim for it on a later rather than an earlier occasion. The changes will prevent a possibly significant future loss of tax.

47 Changes will be made to the definition of the range of bonds exempt from charges on capital gains. Bonds convertible into shares of a quoted parent company will cease to be exempt. Bonds convertible into exempt bonds will themselves be exempt. These changes will counter possible developments which could lead to a significant loss of tax.

48 Shares acquired under the business start-up scheme will be excluded from the arrangements for share pooling.

49 The provisions enabling tax to be deferred where gains are unremittable to the United Kingdom will be amended to make it clear that the relief is available where the unremittability arises in the country where the assets concerned are situated.

Oil taxation

50 A more comprehensive definition of oil field abandonment costs allowable for petroleum revenue tax (PRT) purposes will be introduced. PRT and corporation tax relief will be given on the costs of obtaining guarantees of field abandonment costs. PRT and corporation tax relief will be given where participators in a field meet the abandonment costs of a fellow participator defaulting on his obligations.

51 Doubts about the law on taking PRT penalties by proceedings before the Special Commissioners will be removed.

Inheritance tax

52 The increase in the threshold is in line with the statutory indexation provisions (based on the increase of 9·3 per cent in the RPI in the year to December 1990). The estimated full year cost of indexation attributable to taxable estates in 1991–92 is £125 million.

Stamp duties

53 Under the Finance Act 1990 the abolition date for the duties on securities is to be appointed by Treasury order; it will coincide as closely as possible with the introduction of the Stock Exchange's new system for paperless share transfers (TAURUS). Abolition was previously assumed to take effect from 1 January 1992. Following the Stock Exchange's announcement of a postponement of the introduction of TAURUS, it is now assumed to take effect from 1 April 1992. The yield shown is the additional effect that results from this postponement. Table 4A.1 shows the latest estimate of the effect on receipts on the basis of the previous assumption that abolition took effect from 1 January 1992.

54 Stamp duties on transfers of property other than land and buildings will be abolished from the same date as the duties on securities, assumed to be 1 April 1992. The duty on Northern Ireland bank notes will be abolished from 1 January 1992.

Value added tax

55 The standard rate of VAT will be increased from 15 per cent to $17\frac{1}{2}$ per cent from 1 April 1991.

56 The turnover limit for VAT registration will be raised from £25 400 to £35 000 from 20 March 1991, and the deregistration threshold from £25 400 to £33 600 from 1 May 1991.

57 The waiting period for relief on bad debts written off in traders' accounts will be reduced from two years to one year from 1 April 1991.

58 The rate of serious misdeclaration penalty will be temporarily reduced from 30 per cent to 20 per cent from 20 March 1991 pending the outcome of a review of the penalty. In addition, a period of grace will be introduced during which penalties will not normally be applied on errors found by Customs in the latest accounting period; and a penalty will not normally be charged where a mistake is cancelled out by a mistake in the next return with no overall loss of VAT.

59 From a date to be announced the turnover threshold for annual accounting will be raised from £250 000 to £300 000; there will also be increases in the threshold for using some retail schemes, the limit below which less detailed tax invoices may be issued by retailers, and the limit below which a tax invoice is not required for payments or purchases through a coin-operated machine.

60 From 1 April 1991 VAT relief for charities will be extended to television, radio and cinema advertising; the sale of donated goods by all charities; one-off fund-raising events by charities' trading subsidiaries; donated medical and scientific equipment used in veterinary research; and certain donated equipment directly used in veterinary research.

61 From Royal Assent group treatment will be extended to overseas companies established in the UK.

62 The right of businesses to reclaim VAT on mileage allowances paid to employees to cover road fuel bought for business use will be put on a statutory basis.

63 Taxpayers who pay too much VAT as a result of official error will have a statutory entitlement to interest on the VAT overpaid, from Royal Assent. Such payments are currently made ex-gratia from Vote and will in future be made out of Revenue. The effect shown is the cost to Revenue, but there is a corresponding saving to public expenditure of £5 million.

Car tax

64 The existing relief from car tax for cars supplied for leasing to the handicapped will be extended from Royal Assent to cover leasing agreements which end within three years.

65 From Royal Assent cars used by or on behalf of a car tax registered person for the purposes of commercial or industrial research will be relieved from car tax.

Excise duties

66 Price effects shown below are for the increase in excise duties (and consequential VAT at 15 per cent) from 19 March. The increased VAT standard rate will apply from 1 April. The duties on cigarettes, cigars, hand-rolling tobacco and pipe tobacco will be increased by 15 per cent. The increases in duty plus VAT are equivalent to about 16p on a packet of 20 cigarettes, about 8p on a packet of five small cigars, about 24p on a 25 gram packet of hand-rolling tobacco and about 11p on a 25 gram packet of pipe tobacco.

67 The duty on leaded petrol will be increased by 15 per cent, equivalent to an increase in duty plus VAT of 3·9p a litre.

68 The duty on unleaded petrol will be increased by 15 per cent, equivalent to an increase in duty plus VAT of 3·4p a litre. The tax differential in favour of unleaded petrol will consequently rise from 3·3p to 4·0p a litre.

69 The duty on derv will be increased by 15 per cent, equivalent to an increase in duty plus VAT of 3·3p a litre.

70 The duty on gas oil and fuel oil will rise by 9·3 per cent, equivalent to about 0·1p a litre. This is exclusive of VAT since gas oil and fuel oil supplied to domestic users are zero-rated.

71 The duty on typical beer will be increased by 9·3 per cent, equivalent to an increase in duty plus VAT of about 2p a pint. Duty on beer will be levied on the finished product, instead of the "worts", from a date beyond 1991–92 to be announced later.

72 The duties on wine and made-wine will be increased by 9·3 per cent, equivalent to an increase in duty plus VAT of about 9p on a 75cl bottle of still wine, about 15p on a 75cl bottle of sparkling wine, about 14p on a 70cl bottle of sherry and about 18p on a 75cl bottle of port.

73 The duty on spirits will rise by 9·3 per cent, equivalent to an increase in duty plus VAT of about 56p on a 75cl bottle of spirits.

74 The duty on cider and perry will be increased by 9·3 per cent, equivalent to an increase in duty plus VAT of about 1p a pint.

75 The rate of pool betting duty will be reduced from 40 per cent to 37½ per cent, for a period of four years, provided that the pools promoters pass the full amount saved to a new foundation to be used for the benefit of sports and the arts together with a further contribution of twice that amount which they will collect. The cut in the rate of duty is assumed to take effect from 1 August 1991; it will be conditional upon satisfactory arrangements being made, including the terms and conditions for a trust.

76 Gaming licence duty will be restructured from 1 October 1991. Casinos will be required to make quarterly interim payments of duty based on accrued gross gaming yield, with liability being finally assessed half-yearly. The duty band thresholds will be raised by 20 per cent, so that duty will be payable at the rate of 2½ per cent on the first £450 000 of gross gaming yield for each half-year; 12½ per cent on the next £2 250 000; 25 per cent on the next £2 270 000; and 33⅓ per cent on any remainder. The fixed amount of duty payable on application for a gaming licence will be reduced from £250 to £10.

77 A new category of excise trader, to be known as a registered excise dealer and shipper, will be established. Registration with Customs and Excise will allow a trader to import and pay excise duties on goods from other EC countries outside the bonded warehousing system. Registration will take place during 1992 to become effective from 1 January 1993 on completion of the Single Market.

Vehicle excise duties

78 Duty on cars, buses, lorries and most other vehicles will remain unchanged. Mine rescue vehicles will be exempt from duty. Private fire engines will be subject to the rate of duty on cars. Pedestrian-controlled mowing machines will cease to be liable to registration and licensing.

79 The duty on motorcycles will be raised from £10, £20 and £40 (according to engine capacity) to £15, £30 and £50, with effect from 20 March 1991.

80 The two duty rates for tricycles of £10 and £40 will be replaced by one rate of £50, with effect from 20 March 1991.

81 Duty on special machines (agricultural machines, mobile cranes and similar vehicles) will be increased from £16 to £30, and on recovery vehicles from £50 to £75, with effect from 20 March 1991.

National insurance contributions

82 Employers' contributions on the private benefit of cars they provide for employees will be introduced from 1991–92 at the employers' main rate (10·4 per cent for 1991–92). Contributions will be assessed annually, and collected in the following year. They will be based on the income tax car benefit scales. Employees will be exempted from contributions.

83 Employers' existing liability to contributions on the benefit of free fuel made available for employees' private use will be assessed using the income tax fuel scales from 1991–92. Contributions on free fuel will no longer be payable by employees. The estimated yield is net of contributions that would have arisen under existing legislation.

84 For deductions made after 6 April 1991, employers whose average monthly PAYE/NIC bill is less than £400 will be allowed to make payments to the Inland Revenue quarterly rather than monthly. This line shows the effect on receipts of national insurance contributions. The effect on income tax receipts is at line 18 in Table 4.1.

Community charge

85 The community charge for 1991–92 will be reduced throughout Great Britain by £140. Domestic rates in Northern Ireland will also be reduced. The cost shown is the effect on receipts of the reduction in the community charge and in Northern Ireland rates, net of savings on reliefs and rebates.

Direct effects of previous Budget measures

Table 4A.1 and the accompanying notes show the changes in receipts from major measures enacted in the Finance Act 1990 which are not due to come into effect until 1991–92. The estimates assume that all the measures take effect on the timetable outlined in the Financial Statement and Budget Report (FSBR) 1990–91, and are based on the same conventions as Table 4.1.

Table 4A.1 **Direct effects of previous Budget measures**

	£ million Changes from an indexed base Estimated effect on receipts in: 1991–92	1992–93
Abolition of composite rate tax from 6 April 1991	+350	−400
Abolition of stamp duty on securities from 1 January 1992	−120	−930
Revised VAT bad debt relief provisions from 1 April 1991	−150	−190

Composite rate tax In the FSBR 1990–91 it was estimated that receipts in 1991–92 would be about £550 million higher than if composite rate tax had remained in place, with a shortfall of similar size in 1992–93. The revised estimates reflect changes in the underlying forecast, and increases in the amount of interest likely to be paid gross in the light of detailed arrangements for the registration scheme agreed with the institutions, with consequent reductions in repayments in subsequent years.

Stamp duties on securities The FSBR 1990–91 estimated that, assuming abolition from 1 January 1992, the cost of this measure in 1991–92 would be £120 million and the full year cost £800 million. Table 4A.1 shows the present estimate had abolition remained on the same timetable. Both the 1991–92 and full year costs are unchanged. Abolition of the duties on securities is expected to have some impact on the value of share transactions and the consequential effects on stamp duties and other taxes (such as capital gains tax) are included in the figures, as they were in the FSBR 1990–91 estimates. Some of the additional receipts from these other taxes will only be received after 1992–93. Consequently, the estimated cost in 1992–93 of £930 million is greater than the expected net full year cost of £800 million.

In view of the Stock Exchange's recent announcement about the likely implementation date for its new system for paperless share transfers (TAURUS), it is now assumed that the duties will be abolished from 1 April 1992. The additional yield from this postponement is shown at line 53 of Table 4.1.

VAT bad debt relief The Finance Act 1990 introduced a comprehensive bad debt relief scheme under which traders are able to claim relief on any debt which has been written off in the trader's account and which is two years old. The scheme applies to debts incurred from 1 April 1989 and so claims cannot be made until 1 April 1991.

The estimated costs are for the scheme as proposed in 1990. The cost in 1991–92 has not changed from that published in the FSBR 1990–91. The additional cost of halving the waiting period to one year is shown at line 57 of Table 4.1.

Annex B to Chapter 4

Tax allowances and reliefs

4B.1 This annex provides estimates of the revenue cost of some of the main tax allowances and reliefs. The larger the reliefs, the higher rates of tax have to be in order to finance Government expenditure, other things being equal. And in some cases the reliefs may be relevant in the context of expenditure decisions; tax reliefs may be an alternative to public expenditure, and in this case are often termed " tax expenditures ". In some cases there may be a choice between giving relief as an allowance or deduction against tax, or by an offsetting cash payment (as in the previous investment grant arrangements and in the present MIRAS scheme).

4B.2 Many exemptions and deductions can reasonably be regarded as an integral part of the tax structure. Some do no more than recognise the expenses incurred in obtaining income. Others reflect a more general concept of " taxable capacity ": the personal allowances are a good example. To the extent that income tax is based on ability to pay, it does not seek to collect tax from those with the smallest incomes. But even with structural reliefs of the latter kind, the Government has some discretion about the level at which they are set.

4B.3 Many other reliefs combine both structural and discretionary components. Capital allowances, for example, provide relief for depreciation at a commercial rate as well as an element of accelerated relief. It is the latter element which represents additional help provided to business by the Government, and is a " tax expenditure ". The estimates in Table 4B.1 below show the total cost of the relief and do not distinguish the element which can be regarded as a " tax expenditure ".

4B.4 Other reliefs are more evidently designed to support particular policy objectives, for example the reliefs for owner occupation, for the Business Expansion Scheme, or the new relief in the Budget for training.

4B.5 The loss of revenue associated with tax reliefs and allowances cannot be directly observed, and estimates have to be made. This involves calculating the amount of tax that individuals or firms would have had to pay if there were no exemptions or deductions for certain categories of income or expenditure, and comparing it with the actual amount of tax due. The Government regularly publishes such estimates for Inland Revenue taxes, most recently in Appendix D of the Statistical Supplement to the 1990 Autumn Statement. Largely because of the difficulties of estimation, the published table does not provide a comprehensive coverage of all reliefs.

4B.6 The estimated costs for 1990–91 of some of the main Inland Revenue allowances and reliefs are reproduced in Table 4B.1. In many cases the estimated costs are extremely tentative, and based on simplifying assumptions. The figures are not directly comparable with those in Table 4.1; for example, they are on an accruals basis rather than a receipts basis. But more importantly, they make no allowance for the fact that changes in tax reliefs may cause people to change their behaviour. For example, removing the tax privileges of one form of saving may lead people to switch to another tax privileged form of saving.

4B.7 Table 4B.1 also gives details of reliefs relating to VAT which is collected by Customs and Excise. It shows the estimated yield foregone in 1990–91 by not applying the standard rate of VAT to goods and services which are currently zero-rated. The figures are preliminary estimates and must be treated with caution. In line with the treatment of Inland Revenue taxes, they make no allowance for changes in behaviour.

4B.8 The estimated costs of reliefs and allowances given in Table 4B.1 cannot be added up to give a meaningful total. In some cases this reflects the particular tax regime in operation; for pensions, for example, withdrawal of all the tax reliefs would imply a significant and unrealistic degree of multiple taxation. In other respects it simply reflects the interaction of different reliefs; for example, many more taxpayers would be charged at the higher rate of 40 per cent, and the value of their tax reliefs would be correspondingly higher, if there were no personal allowances.

Table 4B.1 Tax allowances and reliefs: estimated costs in 1990–91

	£ billion
Personal tax	
income tax allowances	30·6
mortgage interest relief	7·8
life assurance premiums[1]	0·3
pension schemes, relief for:	
—employees' contributions	2·2
—employers' contributions	3·8
—investment income of occupational schemes	4·9
—lump sum payments to pensioners	1·0
—personal pensions	1·1
other savings[2]	0·9
employee participation[3]	0·3
charities[4]	0·8
capital gains tax:	
—annual exemptions	0·3
—main residence relief	3·0
Business tax	
capital allowances	
—public corporations	0·5
—North Sea oil and gas production	1·1
—other companies and self-employed	9·5
double taxation relief[5]	2·0
VAT zero rates[6]	
food	5·3
domestic fuel and power	1·8
private sector dwelling	1·5
passenger transport	0·9
books, newspapers etc	0·7
children's clothing	0·5
other[7]	1·1

[1] *For policies taken out before 14 March 1984.*
[2] *Includes various National Savings instruments, BES, PEPs, SAYE and TESSAs.*
[3] *Includes approved profit sharing schemes, savings-linked share option schemes, share option schemes and profit-related pay.*
[4] *Includes reliefs under income tax, inheritance tax and VAT.*
[5] *For accounting periods ending 1987–88.*
[6] *Not all expenditure under these headings is zero-rated.*
[7] *" Other " includes sewerage services and water, drugs medicine and aids for the handicapped and caravans and houseboats.*

Detailed notes for Inland Revenue taxes are provided in Appendix D of the Statistical Supplement to the 1990 Autumn Statement (Cm 1520), from which these figures have been taken with the exception of " capital allowances " where they also reflect the reduction in the main rate of corporation tax for 1990–91 announced in the Budget.

5 Public expenditure

5.01 The Government's expenditure plans for the next three years were announced in the 1990 Autumn Statement (Cm 1311) and set out in detail in Departmental Reports and the Supplement to the Autumn Statement (Cm 1501–1520). Changes announced in January and in the Budget are incorporated in the plans set out in Table 5.1.

Table 5.1 Public expenditure[1]

	£ billion				
	1989–90 Outturn	1990–91 Estimated outturn	1991–92 Plans	1992–93 Plans	1993–94 Plans
Central government expenditure[2]	**127·5**	**140·6**	**152·1**	**161·6**	**167·9**
Of which:					
Department of Social Security	46·9	51·8	58·2	62·6	66·7
Department of Health and OPCS	19·9	22·5	24·9	26·3	27·5
Ministry of Defence	20·8	22·1	22·8	23·4	23·4
Scotland	4·4	4·9	5·8	6·0	6·2
Wales	1·9	2·2	2·5	2·6	2·7
Northern Ireland	5·7	5·9	6·4	6·8	7·1
Other departments	27·9	31·9	31·5	33·9	34·3
Overseas contributions to cost of Gulf conflict		−0·7			
Central government support for local authorities[1]	**38·4**	**42·6**	**52·5**	**55·7**	**56·6**
Of which:					
revenue/rate support grant	13·0	13·1	13·6		
non-domestic rate payments	11·4	12·1	14·3	49·9	50·7
current specific grants	9·7	12·2	18·9		
capital grants	0·9	1·1	1·5	1·5	1·5
credit approvals	3·4	4·0	4·3	4·3	4·4
Financing requirements of nationalised industries	**1·1**	**2·5**	**2·3**	**2·1**	**2·0**
Privatisation proceeds	**−4·2**	**−5·3**	**−5·5**	**−5·5**	**−5·5**
Reserve			**3·5**	**7·0**	**10·5**
Planning total[1]	**162·9**	**180·4**	**205·0**	**221·0**	**231·5**
Local authority self-financed expenditure[3, 4]	14·5	14·7	9·1	9½	11½
Central government debt interest[4]	17·8	17·6	16·7	17	17½
Other adjustments[4]	4·2	3·4	3·9	5	5½
General government expenditure	**199·4**	**216·0**	**234·8**	**252**	**266**

[1] *Following the announcements of extra support for local authorities to reduce community charges the planning total has been increased by £4·7 billion in 1991–92 and by some £6·0 billion and £5·4 billion in the following two years. See paragraphs 5.02 to 5.06 and Table 5.2.*

[2] *Includes the financing requirements of public corporations other than the nationalised industries. See paragraph 4.2 of the Supplement to the 1990 Autumn Statement (Cm 1520).*

[3] *Local authority self-financed expenditure is the difference between total local authority expenditure and central government support for local authorities. Total local authority expenditure is estimated at £52·9 billion and £57·2 billion respectively in 1989–90 and 1990–91. For 1991–92 to 1993–94 it is projected at £61·7 billion, £65½ billion and £68½ billion.*

[4] *1992–93 and 1993–94 figures rounded to nearest £½ billion.*

The reduction in the community charge

5.02 In the Budget, the Chancellor of the Exchequer announced that additional central government support would be provided to local authorities in order to reduce the community charge. This is to be financed from central taxes as described in the box in Chapter 4 (page 43).

5.03 The Government will pay a new grant called the Community Charge Grant which will reimburse authorities for the gross cost of reducing charges in 1991–92 by £140, estimated at some £5·6 billion. It will not be possible to finalise the exact amount payable until after the end of the financial year. So it is proposed to pay 90 per cent of the estimated grant in 1991–92, with the remainder to follow in 1992–93. Payments of community charge grant in respect of 1991–92 are therefore expected to be some £5 billion in that year and £0·6 billion in 1992–93. But the full benefit to chargepayers will come through in 1991–92 and the phasing of the grant payments will not affect the PSBR in either year.

5.04 The net cost of the measure will be lower than payments of the new grant because the reduction in the community charge will bring down the costs of the community charge reduction scheme, announced on 17 January, and of community charge benefit. It is estimated that these savings may bring down the cost of the measure by nearly a quarter, to a net level of some £4·3 billion. This is in line with the estimated fall in the yield of the community charge shown in Table 4.1.

5.05 Provision for support to local authorities in 1992–93 and 1993–94 has also been increased by an amount equivalent to the new grant, uprated in line with the GDP deflator, less estimated savings on the community charge reduction scheme and community charge benefit.

5.06 The public expenditure planning totals for all three years have been increased to take account of these changes and of the community charge reduction scheme and the other measures announced on 17 January. But this additional support from central government has no net effect on the wider aggregate, general government expenditure, since local authority self-financed expenditure is correspondingly reduced. Table 5.2 summarises the changes in the planning total.

Table 5.2 Changes to the planning total[1]

	£ billion		
	1991–92	1992–93	1993–94
Community charge grant	5·0	0·6	
Revenue support grant		5·8	6·0
Savings on reduction scheme and benefit	−1·3	−1·3	−1·4
Net additions as a result of Budget measures[2]	**3·7**	**5·0**	**4·6**
Additions following January announcements	0·9	1·0	0·8
Total additions to planning total	**4·7**	**6·0**	**5·4**

[1] *Changes from the Supplement to the 1990 Autumn Statement.*

[2] *The profile is affected by payment of part of community charge grant in 1992–93 and thus differs from the change in community charge receipts given in Table 4.1. See paragraphs 5.03 and 5.04.*

Other Budget measures

5.07 In October 1991 child benefit will be increased by £1 a week for the eldest eligible child in each family, and 25p a week for all other children. Corresponding increases will be made in income support so that the poorest families will also gain. The impact on public expenditure will be about £220 million in 1991–92 and some £450 million in a full year. This will be charged to the Reserve and will not add to planning totals. In April 1992 and in each subsequent year child benefit will be uprated in line with inflation. Some additional VAT will fall on central government programmes as a consequence of the increase in the rate. The total amount is estimated to be around £450 million. In general this is to be absorbed within existing provision; where this is not done, it will be taken as a charge on the Reserve and will not add to the planning total.

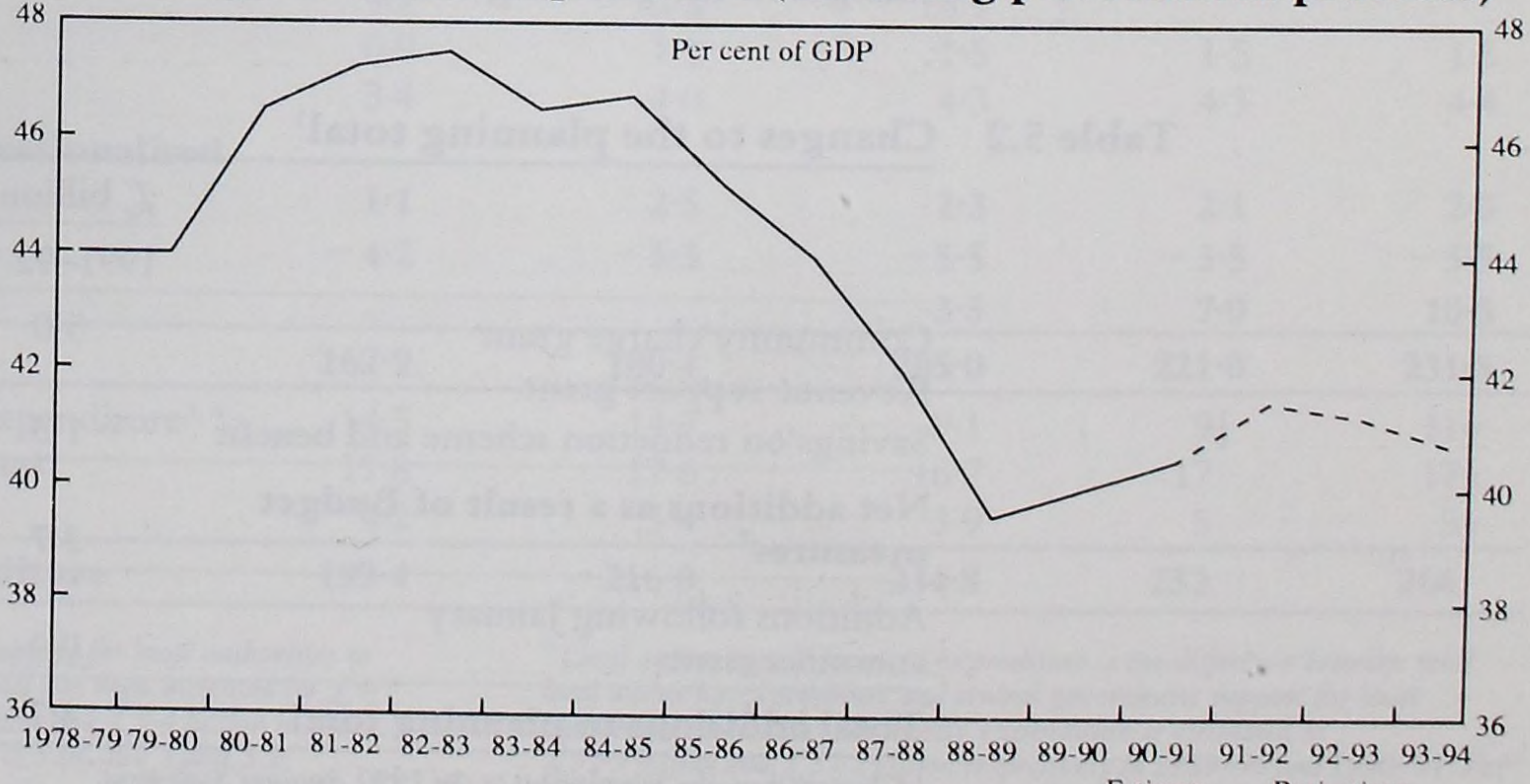
Projections of general government expenditure

5.08 The projections of general government expenditure in Table 5.1 take account of the latest information on local authority budgets for 1991–92. Total local authority spending next year is now expected to be £61·7 billion, compared with £61 billion in the Supplement to the 1990 Autumn Statement. The levels of local authority spending for the following two years have been projected forward using assumptions about real growth similar to those made in the Supplement. Central government debt interest projections have been increased from those set out in the Supplement to reflect the latest fiscal projections.

Public spending trends

5.09 General government expenditure (excluding privatisation proceeds) fell as a proportion of GDP from $47\frac{1}{2}$ per cent in 1982–83 to 40 per cent in 1989–90. Table 5.3 shows the projected path of real GGE and the GGE ratio up to 1993–94 taking account of the new assumptions about money GDP, shown in Chapter 2. The ratio of GGE (excluding privatisation proceeds) to GDP is now expected to be $40\frac{1}{2}$ per cent in the current year. The ratio is projected to be $41\frac{1}{2}$ per cent in 1991–92, falling to $40\frac{3}{4}$ per cent by 1993–94. Chart 5.1 shows the GGE ratio between 1978–79 and 1993–94. The projections in the Medium Term Financial Strategy in Chapter 2 show a further fall in the ratio in 1994–95, to 40 per cent.

Chart 5.1 General government expenditure (excluding privatisation proceeds)[1]



[1] *Figures for the ratio up to 1989–90 are calculated using money GDP figures adjusted to remove the distortion caused by the abolition of domestic rates. See footnote to Table 5.3.*

Table 5.3 General government expenditure

	£ billion				
	1989–90	1990–91	1991–92	1992–93	1993–94
General government expenditure, excluding privatisation proceeds:					
cash	203·6	221·4	240·3	258	272
real terms[1]	203·6	205·3	208·2	214	218
per cent of GDP[1]	40	$40\frac{1}{2}$	$41\frac{1}{2}$	$41\frac{1}{4}$	$40\frac{3}{4}$

[1] *The ratio for 1989–90 is calculated on an adjusted basis to remove the discontinuity caused by the abolition of domestic rates. Real term figures (base year 1989–90) are produced by deflating the cash series by the GDP deflator similarly adjusted. See paragraphs 7 to 12 of Appendix A to the Supplement to the 1990 Autumn Statement (Cm 1520).*

1990–91 outturn

5.10 Table 5.4 sets out the estimated outturn for the planning total in 1990–91, by spending sector. The estimated outturn, which is still subject to some uncertainty, is £180·4 billion. This represents an increase of £1·4 billion above the plans shown in the 1990 Budget. But it is £0·2 billion lower than the forecast in the Autumn Statement and £0·8 billion lower than the estimated outturn in the Supplement to the 1990 Autumn Statement, reflecting cash contributions from other countries towards the United Kingdom's military expenditure in the Gulf.

5.11 So far, other Governments have paid or pledged £1·2 billion in cash contributions towards the UK's additional costs arising from the Gulf conflict. Of this total, £0·7 billion is expected to be paid in 1990–91, and this is taken into account in the estimated outturn for the planning total. The net public expenditure cost in 1991–92 as a result of the Gulf conflict is uncertain. Both additional costs and contributions paid in that year are expected although at this stage neither can be estimated with precision.

Table 5.4 Comparisons of plans and estimated outturn for 1990–91, by spending sector

	£ billion		
	Plans[1]	Estimated outturn	Outturn minus plans
Central government expenditure[2]	138·7	140·6	1·9
Central government support for local authorities	41·8	42·6	0·8
Financing requirements of nationalised industries	0·5	2·5	2·0
Privatisation proceeds	−5·0	−5·3	−0·3
Reserve	3·0	—	−3·0
Planning total	**179·0**	**180·4**	**1·4**

[1] *Plans from The Government's Expenditure Plans 1990–91 to 1992–93, Cm 1021, adjusted for classification changes.*
[2] *See footnote 2 to Table 5.1.*

5.12 The major changes in 1990–91 between the programme plans in the 1990 White Paper and the estimated outturn are:

Central government: higher defence spending, largely on account of the Gulf conflict (£0·9 billion); increased housing expenditure (£0·6 billion), mainly higher subsidies; higher agricultural market support by the Intervention Board (£0·4 billion); and higher health spending (£0·4 billion) largely for pay settlements for NHS Review Body groups. These increases are partially offset by cash contributions from other governments towards Gulf costs (£0·7 billion).

Support for local authorities: increased grant for housing benefit and community charge benefit (£0·6 billion).

Financing requirements of the nationalised industries: increased finance for the electricity industries before privatisation (£1·0 billion), for British Coal (£0·5 billion) and for British Rail (£0·4 billion).

Composition of the planning total

5.13 About three quarters of the planning total will be voted by Parliament. Voted expenditure covers the spending of government departments for their own activities, their funding of other bodies such as the National Health Service and most of central government's support for local authorities. Most of the rest consists of social security benefits paid out of the National Insurance Fund.

5.14 Table 5.5 shows voted and other expenditure by spending sector for 1989–90 and 1990–91, together with the plans for future years set out in the Supplement to the 1990 Autumn Statement. Figures for future years have been adjusted to reflect the changes announced in the Budget.

Table 5.5 The planning total[1]: voted and other expenditure by spending sector

	£ billion				
	1989–90 Outturn	1990–91 Estimated outturn	1991–92 Plans	1992–93 Plans	1993–94 Plans
Central government expenditure[2]	**127·5**	**140·6**	**152·1**	**161·6**	**167·9**
Of which:					
Voted in Estimates	89·3	99·6	108·0	112·7	116·7
Other	38·3	41·0	44·1	49·0	51·3
Central government support for local authorities[1]	**38·4**	**42·6**	**52·5**	**55·7**	**56·6**
Of which:					
Voted in Estimates	33·8	37·5	46·9	na	na
Other	4·6	5·0	5·6		
Financing requirements of nationalised industries	**1·1**	**2·5**	**2·3**	**2·1**	**2·0**
Of which:					
Voted in Estimates	5·4	3·9	2·1	2·2	2·2
Other	−4·3	−1·4	0·2		−0·2
Privatisation proceeds	**−4·2**	**−5·3**	**−5·5**	**−5·5**	**−5·5**
Reserve			**3·5**	**7·0**	**10·5**
Planning total[1]	**162·9**	**180·4**	**205·0**	**221·0**	**231·5**

[1] *The figures for 1991–92 to 1993–94 have been adjusted to take account of the changes announced in the Budget and the introduction of the community charge reduction scheme. See Table 5.2. The proxies for non-domestic rate payments in England and Wales in 1989–90 (£10·1 billion) are treated as if they had been voted in Estimates, to match their treatment from 1990–91. For 1992–93 and 1993–94 plans have been set for the total of revenue support grant and non-domestic rate payments combined. In England and Wales all payments from the non-domestic rates pool are voted but in Scotland local authorities continue to receive business rates direct from business rate payers.*

[2] *Includes the financing requirements of public corporations other than the nationalised industries as follows:*

1989–90	1990–91	1991–92	1992–93	1993–94
0·8	1·1	1·2	1·1	1·3

Supply Estimates

5.15 The total main Estimates provision for 1991–92 for which the Government is seeking Parliamentary approval is shown in Table 5.6. The Estimates were published in a series of booklets on 12 March 1991, with a Summary and Guide (Cm 1454) which explains how they relate to the planning total and describes the Supply procedure. Subject to Parliament's approval of the necessary legislation the Government will in addition be presenting Supplementary Estimates to provide for the additional support to local authorities in 1991–92 announced in the Budget.

5.16 Of the £156·7 billion included in the main Supply Estimates, £153·4 billion is within the planning total. The remaining £3·3 billion is mostly transfers between public sector bodies which do not score in the planning total. Some 63 per cent of the money voted in Estimates is subject to cash limits.

Table 5.6 Supply expenditure[1]

	£ billion			
	1989–90		1990–91	1991–92
	Expected outturn in 1990 Budget	Final outturn	Expected outturn	Provision in main Estimates
Main Supply Estimates	116·5	116·5	138·7	156·7
Supplementaries and net underspending	6·3	5·6	6·9	
Total Supply expenditure	**122·8**	**122·1**	**145·6**	

[1] *This table reflects the actual coverage of the Supply Estimates in each year. Thus no proxies for non-domestic rates in England and Wales are included in the figures for 1989–90. The Supply Estimates from 1990–91 include non-domestic rate payments in England and Wales.*

6 The public sector finances

6.01 This chapter brings together revenue (discussed in Chapter 4) and spending (Chapter 5) and provides an analysis and forecast of the public sector's overall financial position in 1990–91 and 1991–92. It begins with the latest forecasts for the public sector borrowing requirement (PSBR) in 1990–91 and 1991–92 and for the associated stock of debt outstanding. It then explains where the latest forecast for 1990–91 differs from those in the last Budget and Autumn Statement. The remaining sections analyse in more detail:

general government receipts and expenditure;

the behaviour of individual sectors: central government, local authorities and public corporations; and

revenue and expenditure by economic category.

Public sector borrowing requirement and the stock of debt

PSBR **6.02** The latest forecast for PSBR in 1990–91 is a small surplus—a public sector debt repayment—of £0·8 billion, equivalent to $\frac{1}{4}$ per cent of GDP. This follows three years of substantial debt repayments, totalling £26 billion. The estimate for 1990–91 is still subject to considerable uncertainty.

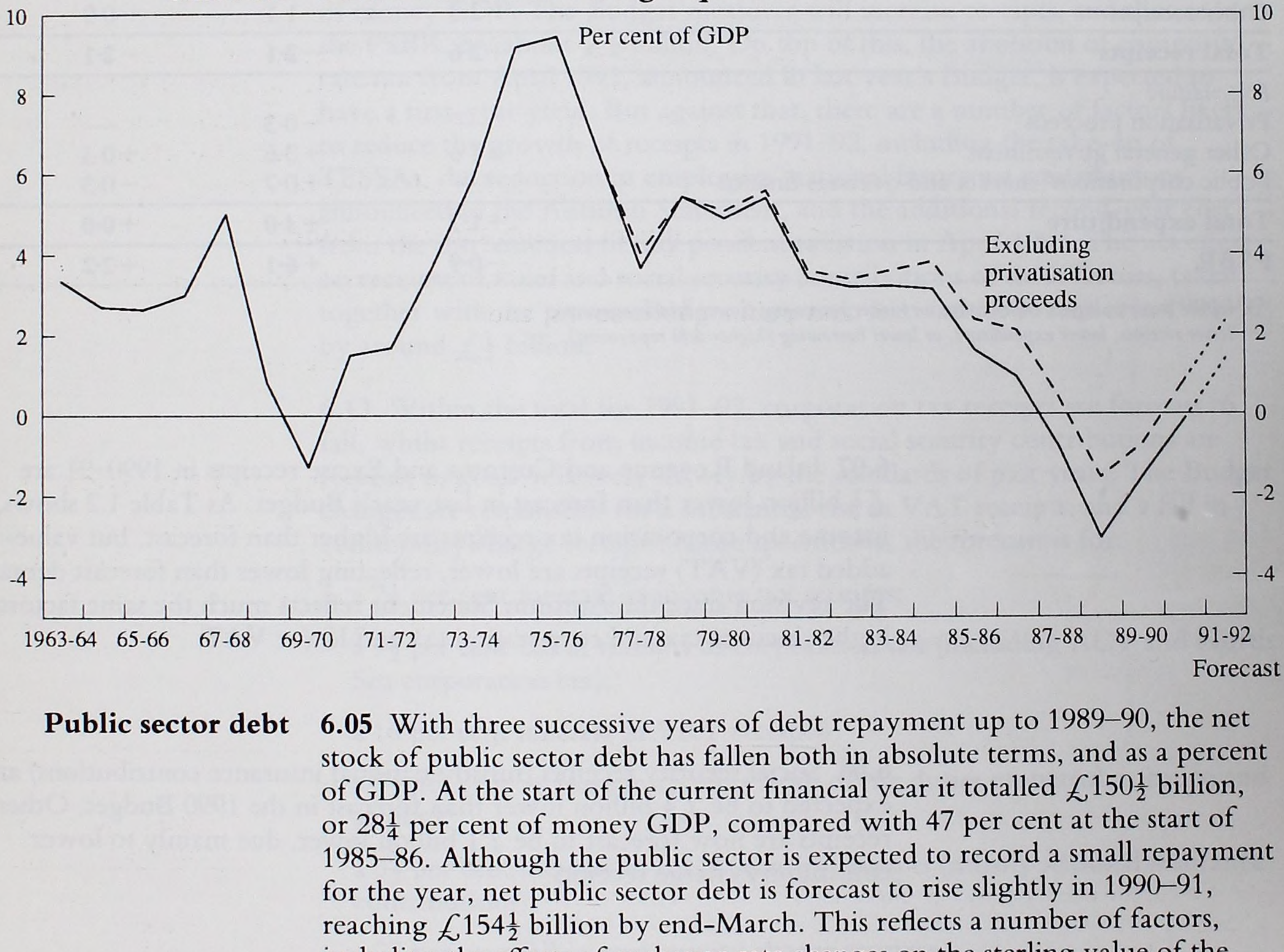
Table 6.1 Public sector borrowing requirement

	1989–90	1990–91		1991–92
	Outturn	1990 Budget	Latest estimate	Forecast
Public sector borrowing requirement				
£ billion	−7·9	−6·9	−0·8	7·9
per cent of GDP	$-1\frac{1}{2}$	$-1\frac{1}{4}$	$-\frac{1}{4}$	$1\frac{1}{4}$
PSBR excluding privatisation proceeds				
£ billion	−3·8	−1·9	4·5	13·4
per cent of GDP	$-\frac{3}{4}$	$-\frac{1}{4}$	$\frac{3}{4}$	$2\frac{1}{4}$

6.03 The fall in economic activity explains much of the move from a debt repayment of $1\frac{1}{2}$ per cent of GDP in 1989–90 to one of only $\frac{1}{4}$ per cent in 1990–91. But there has also been an increase in local authorities' borrowing, which partly reflects delays in collecting community charge and non-domestic rates revenues.

6.04 The impact of recession on the PSBR is likely to be significantly larger in 1991–92 than in 1990–91. But partially offsetting this, there should be a reduction in local authorities' borrowing. Local authority capital spending is expected to fall and authorities will have more experience of collecting the community charge. Authorities will also continue to collect revenues due earlier but not yet received, as well as revenues due in 1991–92. Taking account of all these factors, the PSBR in 1991–92 is forecast at £8 billion, equivalent to $1\frac{1}{4}$ per cent of GDP. Whilst this would be the first borrowing requirement for five years, a PSBR of this size is not large in relation to the figures recorded in the 1960s, 1970s and early 1980s. Moreover, it largely reflects output being below trend.

Chart 6.1 Public sector borrowing requirement



Public sector debt

6.05 With three successive years of debt repayment up to 1989–90, the net stock of public sector debt has fallen both in absolute terms, and as a percent of GDP. At the start of the current financial year it totalled £$150\frac{1}{2}$ billion, or $28\frac{1}{4}$ per cent of money GDP, compared with 47 per cent at the start of 1985–86. Although the public sector is expected to record a small repayment for the year, net public sector debt is forecast to rise slightly in 1990–91, reaching £$154\frac{1}{2}$ billion by end-March. This reflects a number of factors, including the effects of exchange rate changes on the sterling value of the reserves and of inflation on index-linked debt. Nevertheless this forecast implies a further fall in net debt as a percentage of GDP, to $27\frac{1}{2}$ per cent. Despite the move back into deficit, the debt to income ratio should fall again in 1991–92, to around 27 per cent.

Changes since last Budget and Autumn Statement

6.06 The latest forecast for 1990–91 is a public sector debt repayment £6 billion lower than that forecast in last year's Budget and £$2\frac{1}{4}$ billion lower than that forecast in the Autumn Statement. As Table 6.2 shows, the revisions since last year's FSBR are mostly the result of higher expenditure (particularly local authorities' expenditure and debt interest) but receipts are also lower than forecast. The changes since the Autumn Statement, however, are mostly on the receipts side, reflecting weaker than expected activity.

Table 6.2 Changes since 1990 Budget and Autumn Statement[1]

	£ billion		
	Changes since 1990 Budget		Changes since Autumn Statement
	1989–90	1990–91	1990–91
Receipts			
Inland Revenue and Customs and Excise taxes	−0·2	−0·4	−0·5
Social security receipts	+0·2	−0·5	−0·7
Other receipts	+2·5	−1·1	−0·9
Total receipts	**+2·6**	**−2·1**	**−2·1**
Expenditure			
Privatisation proceeds	—	−0·3	—
Other general government	+1·6	+3·6	+0·3
Public corporations' market and overseas finance	—	+0·7	−0·3
Total expenditure	**+1·7**	**+4·0**	**+0·0**
PSBR	**−0·9**	**+6·1**	**+2·2**

[1] + *higher receipts, higher expenditure, or higher borrowing (lower debt repayment);*
− *lower receipts, lower expenditure, or lower borrowing (higher debt repayment).*

6.07 Inland Revenue and Customs and Excise receipts in 1990–91 are £½ billion lower than forecast in last year's Budget. As Table 1.2 shows, income and corporation tax receipts are higher than forecast, but value-added tax (VAT) receipts are lower, reflecting lower than forecast demand. The revision since the Autumn Statement reflects much the same factors; higher income tax and corporation tax and lower VAT.

6.08 Social security receipts (mostly national insurance contributions) are expected to be £½ billion lower than forecast in the 1990 Budget. Other receipts are now forecast to be £1 billion lower, due mainly to lower community charge receipts.

6.09 General government expenditure (GGE) excluding privatisation proceeds is now expected to be £3¾ billion higher in 1990–91 than forecast in last year's Budget. The planning total has been revised up by £1½ billion; local authority self-financed expenditure (LASFE) is £1¼ billion higher and central government debt interest is up by £½ billion. The latest forecast for GGE excluding privatisation proceeds is £¼ billion higher than in the Autumn Statement.

6.10 The position on public corporations' market and overseas finance has also changed significantly since last year's Budget forecast, with the net debt repayment by public corporations now expected to be £¾ billion lower. A lower debt repayment by the electricity companies in the period before privatisation explains most of this change in forecast.

Public sector finances: receipts and expenditure

6.11 Table 1.2 gives the latest estimates for 1990–91, and forecasts for 1991–92, of general government receipts and expenditure, and their components.

Receipts

6.12 General government receipts are estimated to have risen by 5 per cent in 1990–91, about 2 per cent below the growth of money GDP (after adjusting for the effect of the abolition of domestic rates). They are forecast to increase by $4\frac{1}{2}$ per cent in 1991–92, $1\frac{1}{2}$ per cent below the forecast growth of money GDP. The Budget measures will increase receipts, and thus reduce the PSBR, by about £$\frac{1}{4}$ billion. On top of this, the abolition of composite rate tax from April 1991, announced in last year's Budget, is expected to have a first-year yield. But against that, there are a number of factors likely to reduce the growth of receipts in 1991–92, including the take-up of TESSAs, the reduction in employers' national insurance contributions announced in the Autumn Statement, and the additional second-year cost from the introduction of independent taxation in April 1990. The net effect on receipts of taxes and social security contributions of these factors, taken together with the present Budget measures, is to reduce revenues in 1991–92 by around £$\frac{1}{2}$ billion.

6.13 Within the total for 1991–92, corporation tax receipts are forecast to fall, whilst receipts from income tax and social security contributions are forecast to grow relatively slowly by the standards of past years. The Budget changes are responsible for a substantial rise in VAT receipts, and a fall in community charge receipts. More specifically, the forecast is for:

a $7\frac{1}{2}$ per cent increase in income tax receipts;

a $9\frac{1}{2}$ per cent fall in receipts of corporation tax (including ACT and North Sea corporation tax);

a 16 per cent increase in VAT receipts;

a $9\frac{1}{2}$ per cent increase in receipts from excise duties on petrol, tobacco and alcohol;

a $5\frac{1}{2}$ per cent increase in social security receipts (mostly national insurance contributions);

a 27 per cent fall in community charge receipts.

6.14 The projected fall in corporation tax receipts in 1991–92 partly reflects the Budget changes, but most of it is due to the combination of a decline in company trading incomes (net of short-term interest payments) in 1990, and rising capital allowances following on from the high levels of investment in the late 1980s. A projected slowdown in wages and salaries growth is a major factor in the forecast of lower growth in income tax receipts than in the last two years. The forecast fall in real terms in consumer spending in 1991 also means that, without the Budget changes, growth in VAT receipts would have been relatively low.

6.15 North Sea revenues are estimated to have changed little in 1990–91 from the 1989–90 level. Higher oil prices in the second half of 1990 raised the average price for the year above that in 1989 but the tax yield was reduced by the higher levels of investment, in particular by maintenance and safety work. Overall, revenues in 1990–91 were rather lower than forecast in the last Budget. North Sea revenues are forecast to fall substantially in 1991–92, mainly reflecting a sharp drop in petroleum revenue tax (PRT). The level of oil prices and production are both forecast to fall between 1990 and 1991. Investment is forecast to increase, leading in some cases to losses which result in large repayments of PRT. As a share of total taxes, North Sea revenues are forecast to fall to under ¾ per cent—as compared with over 9 per cent in 1984–85 when they were at their peak.

Table 6.3 North Sea revenues

	£ billion			
	1989–90	1990–91		1991–92
	Outturn	1990 Budget	Latest estimate	Forecast
North Sea corporation tax[1]	0·8	1·0	0·8	0·9
Petroleum revenue tax	1·1	1·1	0·9	0·0
Oil royalties	0·6	0·7	0·6	0·5
Total North Sea revenues	**2·4**	**2·8**	**2·3**	**1·4**
[1] *Before ACT set off of:*	*0·5*	*0·5*	*0·4*	*0·5*

Taxes as a share of GDP

6.16 Table 6.4 and chart 6.2 show taxes and social security contributions as a percent of GDP. The total percentage has fallen since 1984–85, but much of this reduction has been due to falling North Sea revenues. Non-North Sea taxes and social security contributions as a percentage of non-North Sea GDP have been broadly flat over this period. The effects of tax cuts on the ratio were largely offset by strong growth in demand, output and profits over much of the period.

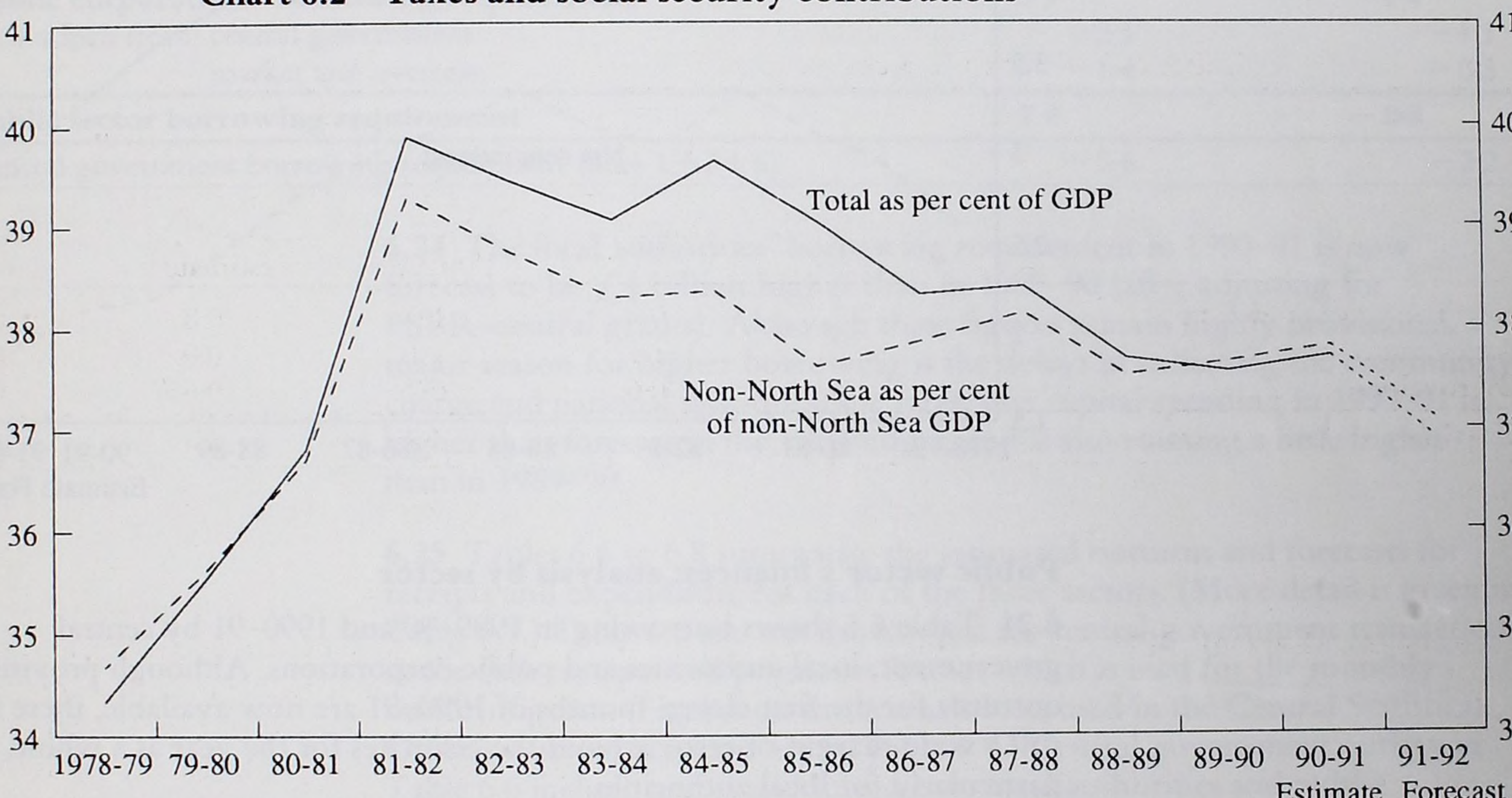
Table 6.4 Taxes and social security contributions as a percent of GDP[1]

	1985–86	1986–87	1987–88	1988–89	1989–90	1990–91 Latest estimate	1991–92 Forecast
Total taxes and social security contributions as a share of total GDP	39	38¼	38½	37¾	37½	37¾	37
Non-North Sea taxes and social security contributions as a share of non-North Sea GDP	37½	37¾	38¼	37½	37¾	37¾	37

[1] *Includes the community charge with taxes from 1989–90.*

6.17 For 1991–92, falls are projected for both the total and non-North Sea ratios. The projected falls largely reflect the cycle; other things equal, the ratio of taxes and social security contributions to GDP falls when economic activity is growing slowly and rises when activity is growing rapidly. Corporation tax receipts in particular are markedly cyclical; the forecast implies a fall in non-North Sea corporation tax receipts as a percent of non-North Sea GDP in 1991–92 of over $\frac{1}{2}$ per cent. On top of this, the rise in money GDP resulting from the Budget increase in VAT reduces the ratio by over $\frac{1}{4}$ percentage point. These two factors more than account for the projected fall in the tax/GDP ratio.

Chart 6.2 Taxes and social security contributions

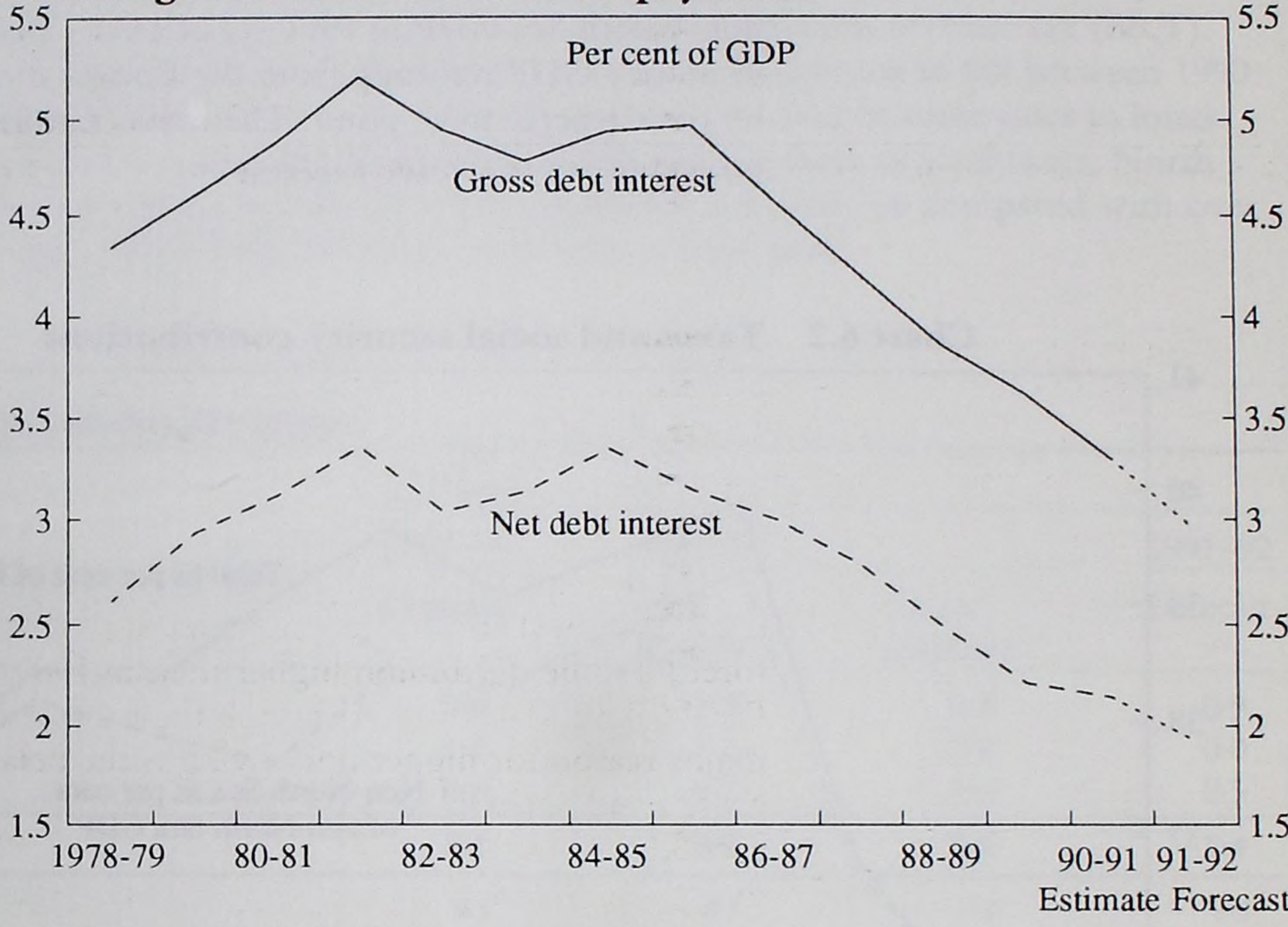


Expenditure **6.18** GGE excluding privatisation proceeds is now estimated to have increased by $8\frac{3}{4}$ per cent in 1990–91, somewhat faster than the growth of money GDP. The ratio of GGE excluding privatisation proceeds is thus estimated to have risen slightly. A rise in the ratio is always likely when activity is weakening, since GGE tends to exhibit rather less variation over the cycle than does output and some key elements, notably social security expenditure, rise when activity weakens. The underlying trend in the ratio since the early 1980s has been clearly downwards; it has fallen from over 47 per cent in the early 1980s to $40\frac{1}{2}$ per cent in 1990–91.

6.19 Since output is not expected to recover until the second half of 1991, a further rise in the ratio of GGE excluding privatisation proceeds to GDP is forecast for 1991–92. (The forecast for the GGE/GDP ratio is shown in Table 5.3.)

6.20 Within GGE, debt interest payments fell in 1990–91, both in cash terms and as a percent of GDP, reflecting a lower stock of debt. Although a return to public sector borrowing is forecast for 1991–92, the forecast shows a further fall in debt interest, both in cash terms and as a percent of GDP.

Chart 6.3 General government debt interest payments



Public sector's finances: analysis by sector

6.21 Table 6.5 shows borrowing in 1989–90 and 1990–91 by central government, local authorities and public corporations. Although provisional outturns for the first eleven months of 1990–91 are now available, there is still a wide margin of error around the estimates for the year as a whole, particularly for local authorities.

6.22 The sectoral positions in both 1989–90 and 1990–91 are affected by substantial, PSBR-neutral, transfers between central government and the other two sectors. In 1989–90, there was a capitalisation grant of £0·9 billion from central government to Scottish local authorities, and a grant of £3·0 billion to British Coal. In 1990–91, there was a further grant of £1·2 billion to British Coal; and a grant of £0·6 billion to Scottish new towns, part of the public corporations sector, is scheduled for March. All these grants were used to repay borrowing from central government; hence the effect of the grants is to increase central government own account borrowing, but to reduce borrowing by local authorities (in the case of Scottish local authorities) or public corporations (in the other three cases) by equal amounts.

6.23 The financial positions of all three sectors showed a deterioration in 1990–91. Excluding the effects of PSBR-neutral grants, the net debt repayment by central government was £5 billion lower than in 1989–90, whilst a debt repayment of nearly £1 billion by public corporations in 1989–90 turned into a borrowing requirement of nearly £$\frac{1}{2}$ billion in 1990–91. In the case of the public corporations sector, the slow down in output has put pressure on nationalised industries' trading surpluses against a background of heavy investment programmes, and has led to higher calls on external finance.

Table 6.5 Public sector borrowing requirement by sector

		£ billion			
		1989–90 Outturn		1990–91 Latest estimate	
1	**Central government borrowing requirement on own account**	**−5·4**		**−2·4**	
2	**Local authority borrowing requirement**	**1·3**		**3·0**	
3	of which from: central government		2·3		1·3
4	market and overseas		−0·9		1·7
5	**Public corporations' borrowing requirement**	**−3·9**		**−1·4**	
6	of which from: central government		−2·5		−1·1
7	market and overseas		−1·4		−0·3
8	**Public sector borrowing requirement**	**−7·9**		**−0·8**	
	Central government borrowing requirement (lines 1+3+6)		−5·6		−2·2

6.24 The local authorities' borrowing requirement in 1990–91 is now forecast to be £$\frac{3}{4}$ billion higher than in 1989–90 (after adjusting for PSBR-neutral grants). Although these figures remain highly provisional, a major reason for higher borrowing is the delays in collecting the community charge and national non-domestic rates. Net capital spending in 1990–91 is higher than forecast in the last Budget, and is also running a little higher than in 1989–90.

6.25 Tables 6.6 to 6.8 summarise the estimated outturns and forecasts for receipts and expenditure for each of the three sectors. (More detail is given in Table 6.9.) Table 6.6 sets out the forecast for central government transactions in the cash receipts and payments format which is used for the monthly outturn figures. (Figures on the accruals basis used in the Central Statistical Office's national accounts are in Table 6.9.) Central government outlays in Table 6.6 include grants and subsidies to local authorities and public corporations, which are correspondingly included in the receipts of these sectors shown in Tables 6.7 and 6.8. The forecast of the PSBR for 1991–92 assumes that the Reserve is fully spent, though the Reserve is unallocated and is not included in the expenditure estimates for individual sectors.

Central Government

6.26 The rise in central government receipts in 1990–91, at 12$\frac{1}{2}$ per cent, was unusually high, reflecting the reclassification of non-domestic rates as a central government tax (scored as other receipts in Table 6.6) from April 1990. The increase in Inland Revenue and Customs and Excise taxes together was smaller, at 7 per cent. The forecast rise in 1991–92 is 5$\frac{3}{4}$ per cent. The reclassification of non-domestic rates also raised net departmental outlays in 1990–91 by broadly the same amount as receipts, as the receipts are passed on to local authorities as part of central government support. Net departmental outlays, excluding any allocation from the reserve, are forecast to rise by 10$\frac{1}{2}$ per cent in 1991–92.

Local authorities

6.27 The net revenue due to be collected by local authorities as non-domestic rates is forecast to increase by 13 per cent in 1991–92. After allowance is made for rebates (the community charge reduction scheme (CCRS) announced in January and community charge benefit) and for the reduction in the community charge announced in the Budget, the net revenue due from the community charge is forecast to be 37 per cent lower than the net revenue due for 1990–91. (These figures are shown in Table 6.7.) In addition to the revenues due for 1991–92, there will be some late collection of revenues due but not paid in 1990–91. As a result

Table 6.6 Central government transactions on a cash receipts basis

	£ billion		
	1989–90 Outturn	1990–91 Latest estimate	1991–92 Forecast[1]
Receipts			
Inland Revenue and Customs and Excise	128·9	138·0	146·1
Social security contributions (GB)	31·0	32·9	34·9
Interest and dividends	9·9	9·5	10·0
Other	3·8	14·6	16·2
Total receipts	**173·5**	**195·0**	**207·1**
Outlays			
Interest payments	16·6	15·9	16·0
Privatisation proceeds	−4·2	−5·3	−5·5
Net departmental outlays	155·7	182·1	201·0
Total outlays	**168·2**	**192·6**	**211·5**

[1] *Excluding any allocation from the Reserve.*

community charge actually collected in 1991–92 (net of CCRS and community charge benefit) is forecast to be 27 per cent lower than that actually collected in 1990–91. This forecast assumes an average community charge—before rebates—in 1991–92 in Great Britain of £245.

Table 6.7 Local authority transactions

	£ billion		
	1989–90 Outturn	1990–91 Latest estimate	1991–92 Forecast
Receipts			
Community charge and domestic rates[1]	9·6	11·5	7·3
Non-domestic rates	11·1	12·5	14·1
Current grants from central government[2]	24·7	27·4	35·4
Capital grants from central government	2·3	2·2	2·9
Other	7·5	4·9	6·9
Total receipts	**55·2**	**58·5**	**66·5**
Expenditure[3]			
Current expenditure on goods and services	39·4	43·5	47·3
Current grants and subsidies	6·5	6·8	8·0
Interest	5·0	5·1	5·5
Capital expenditure and net lending	5·7	6·1	5·5
Total expenditure[4]	**56·5** (52·9)	**61·5** (57·2)	**66·3** (61·7)

[1] *Net of rate rebates, community charge benefit, transitional relief and community charge reduction scheme.*
[2] *Net of non-domestic rate income in 1990–91 and 1991–92.*
[3] *The figures for local authority expenditure in 1991–92 take account of the latest information on local authority budgets. See footnote 3 to Table 5.1.*
[4] *The expenditure figures in this table are on a national accounts basis; the figures in brackets are equivalent figures on the public expenditure measurement basis used in Chapter 5.*

6.28 Local authorities' current expenditure is forecast to increase by 9 per cent in 1991–92. Gross capital spending was high in 1989–90, as a result of authorities spending to forestall the introduction of the new capital finance regime in April 1990. It was expected to fall back in 1990–91, but in the event the actual fall in gross spending has turned out to be smaller than expected at the time of the last Budget. Authorities have been spending a rather larger proportion of their usable receipts than earlier expected. Capital spending is expected to fall back in 1991–92, measured both gross and net of receipts.

Public corporations **6.29** Trends in public corporations' finances have been obscured in recent years by changes in coverage of the sector arising from privatisations. The regional water authorities are excluded from the figures in Table 6.8 from December 1989, the regional electricity companies (England and Wales) from December 1990, and the non-nuclear electricity generating companies (England and Wales) from March 1991. Much of the reduction in public corporations' gross trading surplus shown in Table 6.8 for 1990–91 and 1991–92 can be explained by these changes. Nevertheless, some of the reduction in 1990–91 is attributable to the financial performance of the electricity industries prior to privatisation. The remainder, in both 1990–91 and 1991–92, is largely attributable to the recession. Capital expenditure by the nationalised industries, excluding the electricity industry, is estimated to have risen in 1990–91 and is forecast to rise further in 1991–92.

Table 6.8 Public corporations' transactions

	£ billion		
	1989–90 Outturn	1990–91 Latest estimate	1991–92 Forecast[1]
Receipts			
Gross trading surplus (including subsidies)	5·6	4·0	2·0
Capital grants from central government	4·2	3·3	2·0
Other	2·6	1·5	1·4
Total receipts	**12·4**	**8·9**	**5·4**
Expenditure			
Interest, dividends and taxes on income	3·2	2·5	1·7
Net lending and capital expenditure	5·4	5·0	3·9
Total expenditure	**8·6**	**7·5**	**5·6**
Public corporations' contribution to planning total:			
nationalised industries external finance	*1·1*	*2·5*	*2·3*
other public corporations	*0·8*	*1·1*	*1·2*

[1] *Excluding any allocation from the Reserve*

Public sector's finances: analysis by economic category

6.30 The full analysis of receipts and expenditure by economic category is shown in Table 6.9, with a breakdown between central government, local authorities and public corporations. This analysis, which distinguishes between current and capital transactions (and within the latter between physical and financial investment), shows the derivation of the public sector financial deficit. The financial deficit, unlike the PSBR, is not wholly a measure of cash transactions because certain items above line 25 in Table 6.9, for example some taxes included in lines 1 and 2, are measured on an accruals basis. Accruals adjustments are accordingly made in lines 29 and 30.

6.31 The Reserve is assumed to be spent on transactions that fall above the financial deficit line. In practice allocations from the Reserve can also affect financial transactions (lines 26 to 31).

Table 6.9 Public sector transactions by sub-sector and economic category

£ billion

1990–91 Latest estimate

	Line[1]	General government: Central government	General government: Local authorities	General government: Total	Public corporations	Public sector
Current and capital receipts[2]						
Taxes on income, and oil royalties	*1*	78·5	—	78·5	−0·5	78·0
Taxes on expenditure	*2*	76·6	0·1	76·7	—	76·7
Taxes on capital	*3*	4·2	—	4·2	—	4·2
Social security contributions	*4*	35·4	—	35·4	—	35·4
Community charge	*5*	—	11·4	11·4	—	11·4
Gross trading surplus	*6*	−0·5	0·5	—	4·0	4·0
Rent and miscellaneous current transfers	*7*	0·5	3·3	3·8	0·6	4·4
Interest and dividends from private sector and abroad	*8*	3·8	1·3	5·1	0·7	5·8
Interest and dividends within public sector	*9*	5·9	−4·5	1·3	−1·3	—
Imputed charge for non-trading capital consumption	*10*	1·6	1·9	3·5	—	3·5
Capital transfers	*11*	—	0·1	0·1	0·2	0·2
Total receipts	*12*	**206·0**	**14·1**	**220·0**	**3·7**	**223·8**
Current and capital expenditure[2]						
Current expenditure on goods and services	*13*	68·2	43·5	111·7	—	111·7
Subsidies	*14*	5·9	0·5	6·4	—	6·4
Current grants to personal sector	*15*	57·6	6·3	64·0	—	64·0
Current grants paid abroad	*16*	3·6	—	3·6	—	3·6
Current grants within public sector	*17*	39·9	−39·9	—	—	—
Debt interest	*18*	17·6	0·5[3]	18·1	0·3	18·4
Gross domestic fixed capital formation	*19*	6·5	5·4	11·9	4·7	16·6
Increase in stocks	*20*	0·1	—	0·1	0·2	0·3
Capital grants to private sector	*21*	2·7	0·8	3·5	0·1	3·5
Capital grants within public sector	*22*	5·6	−2·2	3·4	−3·4	—
Total expenditure	*23*	**207·6**	**14·9**	**222·6**	**1·9**	**224·4**
Reserve	*24*	—	—	—	—	—
Financial deficit	*25*	**1·6**	**0·9**	**2·5**	**−1·8**	**0·7**
Financial transactions						
Net lending to private sector and abroad	*26*	0·3	−0·1	0·2	—	0·2
Cash expenditure on company securities (including privatisation proceeds)	*27*	−5·7	0·1	−5·6	−0·1	−5·7
Transactions concerning certain public sector pension schemes	*28*	—	—	—	—	—
Accruals adjustments on receipts	*29*	2·1	1·4	3·5	—	3·5
Other accruals adjustments	*30*	−1·7	−0·2	−1·9	−0·2	−2·0
Miscellaneous financial transactions	*31*	0·9	0·9	1·8	0·7	2·5
Borrowing requirement	*32*	**−2·4**	**3·0**	**0·5**	**−1·4**	**−0·8**

1 *Financial deficit (line 25) = expenditure (line 23) + Reserve (line 24) − receipts (line 12).*
Borrowing requirement (line 32) = financial deficit (line 25) + financial transactions (lines 26 to 31).

2 *On an accruals basis.*

3 *Excludes local authorities' debt interest payments to central government, included in row 9.*

	£ billion					
	1991–92 Forecast					
	General government			Public corporations	Public sector	
Line[1]	Central government	Local authorities	Total			
						Current and capital receipts[2]
1	79·2	—	79·2	−0·1	79·1	Taxes on income, and oil royalties
2	86·9	0·1	87·0	—	87·0	Taxes on expenditure
3	3·6	—	3·6	—	3·6	Taxes on capital
4	37·2	—	37·2	—	37·2	Social security contributions
5	—	7·2	7·2	—	7·2	Community charge
6	−0·6	0·5	−0·1	2·0	1·9	Gross trading surplus
7	0·9	3·3	4·2	0·6	4·9	Rent and miscellaneous current transfers
8	4·1	1·0	5·1	0·7	5·9	Interest and dividends from private sector and abroad
9	6·0	−5·0	0·9	−0·9	—	Interest and dividends within public sector
10	1·7	2·0	3·7	—	3·7	Imputed charge for non-trading capital consumption
11	—	0·1	0·1	0·2	0·3	Capital transfers
12	**219·0**	**9·1**	**228·1**	**2·5**	**230·6**	**Total receipts**
						Current and capital expenditure[2]
13	72·5	47·3	119·9	—	119·9	Current expenditure on goods and services
14	5·7	0·6	6·3	—	6·3	Subsidies
15	63·5	7·4	70·9	—	70·9	Current grants to personal sector
16	3·4	—	3·4	—	3·4	Current grants paid abroad
17	49·4	−49·4	—	—	—	Current grants within public sector
18	16·7	0·4[3]	17·2	0·4	17·5	Debt interest
19	7·3	4·9	12·2	3·9	16·1	Gross domestic fixed capital formation
20	—	—	—	−0·1	−0·1	Increase in stocks
21	3·5	0·7	4·3	0·1	4·3	Capital grants to private sector
22	4·8	−2·9	2·0	−2·0	—	Capital grants within public sector
23	**227·0**	**9·1**	**236·1**	**2·2**	**238·4**	**Total expenditure**
24					3·5	Reserve
25					**11·3**	**Financial deficit**
						Financial transactions
26	0·2	−0·2	—	0·1	0·1	Net lending to private sector and abroad
27	−5·5	—	−5·5	—	−5·5	Cash expenditure on company securities (including privatisation proceeds)
28	0·1	—	0·1	—	0·1	Transactions concerning certain public sector pension schemes
29	2·8	−0·6	2·2	—	2·2	Accruals adjustments on receipts
30	−0·8	−0·1	−0·9	−0·2	−1·0	Other accruals adjustments
31	−0·6	0·7	0·1	0·6	0·7	Miscellaneous financial transactions
32					**7·9**	**Borrowing requirement**

Annex to Chapter 6

Conventions used in presenting the public finances

6A.1 The public finances can be presented in several ways. But broadly speaking, most fall under the heading of either the Central Statistical Office's *national accounts* approach or what can be termed the *cash flows* approach. Cash is of particular interest because the public sector borrowing requirement (PSBR), the main fiscal indicator, is itself almost entirely a cash concept. It measures the public sector's net cash flow position *vis-à-vis* the private and overseas sectors.

6A.2 On the expenditure side of the account there is a further presentation which corresponds with the way public expenditure is planned, controlled and accounted for (see for example Table 5.1). The measurement basis for individual expenditure components of the planning total is closely related to the cash based approach. However the medium term spending objective is based on general government expenditure, which is a national accounts concept.

6A.3 The FSBR utilises all these presentations, the choice depending on the context. This annex gives a brief description of the various presentations and of the relationship between the relevant tables in Chapters 1, 2 and 6.

National accounts approach

6A.4 The *national accounts* approach is based on an internationally agreed framework for measuring economic activity. It is useful because it allows the public finances to be put in the context of the whole economy. It illuminates in particular the inter-relationships with other sectors. This approach distinguishes between current and capital income and expenditure, and shows the resulting financial surplus or deficit. National accounts measurement conventions have some important implications in the context of public finances:

—most transactions, including taxes, are recorded on an *accruals* rather than cash payments basis;

—current and capital transactions are grouped by economic category;

—the value of some transactions is *imputed* where no money changes hands.

6A.5 Table 6.9, which shows the three sub-sectors as well as public sector as a whole, is the main national accounts presentation of public finances in the FSBR. Tables 6.7 and 6.8, on local authorities and public corporations respectively, are essentially summary versions of the relevant columns of Table 6.9. It is possible to define the PSBR in terms of national accounts concepts, as in Table 6.9, even though these include imputed and accrued flows. The imputed flows appear on both sides of the accounts and cancel out when calculating the PSBR, and the financial transactions include an explicit adjustment for the difference between accruals and cash flow (rows 29 and 30 in Table 6.9). One consequence of the inclusion of imputed flows is that the national accounts approach will generally result in higher total gross flows of receipts and expenditure than if cash flows only were recorded.

Cash approach **6A.6** An alternative method of presenting public finances is to concentrate directly on the *cash transactions* actually occurring in a given time period between the public and private or overseas sectors. Everything would then appear on a *receipts or payments* basis. This approach is particularly useful for analysing the components of the PSBR which is itself a cash concept. But whilst the PSBR outturn figures can be calculated on a cash basis from the financing transactions, complete cash data on the income and expenditure components of the PSBR are only available for central government. The cash data available for local authorities or public corporations are not comprehensive.

6A.7 Table 6.6 is a fully cash-based presentation of central government finances. The outturn estimates use information on the cash flows underlying the central government's funds and accounts such as the Consolidated Fund and National Loans Fund. While the table aggregates similar and related transactions across all funds and accounts, the choice of aggregation is limited by the accounting data that is readily available. Further details are given in Treasury Working Paper No. 57.

6A.8 The receipts side of Table 1.2 is as close as possible to a cash-based presentation for the public sector as a whole. All the individual taxes are shown on this basis. Total tax and royalty receipts are on a cash basis, with the exception that "other taxes" includes some VAT refunded to central and local government. Total general government receipts are on a cash basis with the following main exceptions:

—"other" taxes and royalties include some refunded VAT;

—social security contributions include imputed flows for statutory sick and maternity pay, but are otherwise on a cash basis;

—"other" receipts include an imputed flow for capital consumption and an accruals adjustment for debt interest.

6A.9 Inclusion of capital consumption, imputed statutory sick and maternity pay, refunded VAT, and accrued capital uplift on indexed gilts within general government expenditure are the four main departures from cash on the expenditure side of the account in Table 1.2. When translating from the planning total to general government expenditure, the first three are included in the accounting adjustments and the last is in central government debt interest. Further details are in Appendix B of the Supplement to the 1990 Autumn Statement.

Main aggregates **6A.10** The rest of this annex briefly explains the main receipts and expenditure aggregates, concentrating on the different definitions used in the various tables. Tables 2A.1, 2A.3 and 2A.5 are all on the same basis as Table 1.2.

Taxes: taxes are on a cash basis in Tables 1.2 (except "other" taxes which include some refunded VAT) and 6.6, but on an accruals basis in Table 6.9. When looking at taxes (and social security contributions and community charge) as a percent of GDP, as in Tables 6.4 and 2A.2 for example, taxes are measured on an accruals basis. This is because a measure of the underlying burden of taxation is required and not one which may be affected by the vagaries of the precise timing of tax payments. The accrued total of taxes, divided into the three economic categories of income, expenditure and capital, is shown in Table 6.9. The difference between the total of these and that shown in Table 1.2 is included in the accruals adjustment on receipts in Table 6.9.

Social security contributions: these are treated equivalently to taxes except that in Table 1.2 they include imputed flows (see paragraph 6A.8.). Contributions in Table 6.6 differ from those in Table 1.2 in that they exclude Northern Ireland contributions and the imputed flows.

Community charge and rates: these are on a cash basis in Table 1.2 and on an accruals basis in Tables 6.7 and 6.9.

General Government Expenditure (GGE): GGE is derived from the planning total in Table 1.2. Table 6.9 arranges the information in national accounts terms.GGE excluding net lending to public corporations can be obtained from the general government column by taking total expenditure (row 23) and adding (i) the Reserve (row 24), all assumed to be general government; (ii) net lending to the private sector (row 26); and (iii) cash expenditure on company securities (row 27). Net lending to public corporations is shown in Table 6.5.

Central government debt interest payments: these include accrued capital uplift on indexed gilts in Tables 1.2, 5.1 and 6.9, but exclude it in Table 6.6 which measures interest payments on a cash basis.

References

6A.11 Further information on the conventions used in measuring and presenting public finances can be found in:

" United Kingdom National Accounts Sources and Methods " (Third Edition, 1985), Central Statistical Office—especially chapters 9, 10 and 11;

" Financial Statistics Explanatory Handbook ", 1990, Central Statistical Office;

" Central Government Funds and Accounts and the Central Government Borrowing Requirement", Treasury Working Paper No. 57, June 1990.

" Public Expenditure Analyses to 1993–94, Statistical Supplement to the 1990 Autumn Statement ", HM Treasury, February 1991, HMSO Cm 1520.

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