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The British Budget for 1959-60 11 pages

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The British budget for the fiscal year ending March 31, 1960 is designed to give a powerful stimulus to the British economy. Personal disposable income will be increased and consumption directly promoted by tax concessions of £295 million and the return of £71 million in war time forced savings. Government loans and investment outlays are planned to rise by £193 million. Private investment is encouraged through additional depreciation allowances. The over-all budget deficit is expected to rise from £182 million to £721 million.

The budget is more expansionary than most commentators had envisioned. It reflects official disappointment with the slow rate of recovery from last year's recession. Industrial production rose less than 2 per cent from the low of last summer, largely under the impetus of an installment credit boom. Unemployment has been reduced somewhat but remains high by postwar British standards. The authorities believe they have a safe margin for expansion without inflation. Not only are the effects of the recession to be overcome but there is excess capacity in industry as a result of high levels of investment and little growth in recent years. The Government's anti-inflationary policies of September 1957 and the subsequent fall in internal demand led to a significant moderation of the chronic wage price spiral in 1958. In addition, a record balance-of-payments surplus was earned last year in large measure because of the windfall of a 10 per cent reduction in import prices together with inventory adjustments at home. Finally, the authorities were able through bond sales to nonbank investors to regain a substantial measure of control over the banking system.

Because of the margin of labor and capacity available for further expansion, the situation is not fully analogous to the case of the last pre-election budget in 1955. At that time, substantial tax concessions were made in the face of an internal investment boom and a deteriorating balance of payments. Subsequent debt-management and inflationary difficulties forced the Chancellor to introduce an extraordinary fall budget in which he took back much of what he had given away in the spring.

A great deal has already been done to encourage business expansion since the ceiling on bank loans was ended in July 1958, and the effects of much of this program have yet to be felt. Since July, installment credit controls have been removed, the ceiling on public investment lifted, and Capital Issues Controls suspended. Expanded government loan programs were announced for housing, internal transport, and overseas development. Along with the abandonment of many internal controls, the authorities took the occasion of the strong external condition of the pound to remove some of the import controls against dollar goods and, in December 1958, made foreign-held sterling officially convertible on current account.

The total budget

As a result of planned lower revenues and increased expenditures, the over-all budget deficit is forecast to be £721 million compared with an actual deficit of £182 million last year.

Table 1

U.K. Budget

(In millions of pounds)

	1959-60 estimated	1958-59 actual
Current revenues	5,325	5,480
Current expenditures	5,223	5,103
Current surplus	102	377
Net loans for nationalized industries and overseas development; public works	823	559
Over-all deficit	721	182

The budget estimates for 1959-60, before tax cuts, assumed a rise in inland revenue (mainly income taxes) of one per cent and a rise in customs and excise revenues of 2 per cent. On the expenditure side, interest payments on the public debt are assumed to decline by almost 10 per cent or £63 million as a result of the sharp fall in short-term interest rates in the last year. Little change is contemplated in defense outlays. Civil expenditures are planned to rise by only one half of one per cent.

Amount to be borrowed — The amount of deficit to be financed is considerably larger than in 1958-59. The budget, however, is only one of the factors determining Treasury cash needs. Others are the net change in Britain's foreign position, changes in the volume of currency in circulation, and the amount of maturing debt. In the past year, sales of bonds to the nonbank public were sufficiently large to enable the authorities to cover the budget deficit, the maturing debt, and net inflow of foreign exchange and to retire a substantial amount of government bonds and Treasury bills held by the banking system.

In the words of the Chancellor, "The restraint thus exercised over the total of floating debt in the hands of the market considerably strengthens our ability to influence future monetary developments. . . ."1/

Table 2

Treasury: Estimated Cash Needs and Sources

(In millions of pounds)

	1958-59	1959-60
Treasury cash needs:		
Budget deficit	182	721
Increase in official reserves a/	11	--
Debt to banks	325 b/	--
Total	518	--
Maturing marketable debt	1,268	950
Known Treasury sources of cash:		
Increased note circulation	50	--
Net sales National Savings and tax certificates	350	--

a/ Includes net of official reserve increases, increased debt to EPU, and increases in sterling liabilities including estimates for the period January-April 1959.
b/ Mid-April 1958 to mid-April 1959.

The authorities start the coming year in a strong position. As a result of a successful year of sales of small savers and marketable bonds to the nonbank public, they are in a position to exert pressures on the banking system. In the next fiscal year, the deficit to be financed will be much larger; maturing debt requirements will be less but much more new cash will have to be raised. It will be necessary to again make relatively large net sales of bonds to the nonbank public if the authorities are to avoid the need to fall back on Treasury bill sales to the banks to raise the necessary cash.

Revenue concessions in the budget

Income tax cuts -- The principal tax concession is the 9 per cent cut in the standard rate of income tax (from 42-1/2 to 38-3/4 per

1/ Budget Speech, House of Commons, April 7, 1959, Hansard, H.M.S.O. p. 35, 36.

cent) effective June 1. Even larger cuts in rates apply to lower taxable incomes. These reductions are expected to cost £192 million this fiscal year and £229 million in a full year. The standard rate is paid on personal taxable income in excess of £360 and reduced rates apply on taxable income up to this amount. Surtax rates, which range from 10 to 50 per cent on all taxable income in excess of £2,000, remain unchanged. The highest personal income tax (standard plus surtax) rate now becomes 88-3/4 per cent instead of 92-1/2 per cent. Corporations pay the standard rate on their total income, and in addition are subject to a 10 per cent profits tax. The new rate for corporations is thus 48-3/4 per cent instead of 52-1/2 per cent. The reduction in corporate income taxes could mean tax savings on profits put in reserve of some £60 million annually.

Sales (purchase) tax cuts -- Sales tax reductions will cost an estimated £59 million in revenue this fiscal year and £81.5 million in a full year. Three of the sales tax brackets have been reduced as follows: (1) the 60 per cent rate to 50 per cent (mainly autos and TV sets); (2) the 30 per cent rate to 25 per cent (mainly refrigerators, watches and jewelry); and (3) the 15 per cent rate to 12-1/2 per cent (mainly kitchenware, china, etc.). The 5 per cent rate on miscellaneous items is unchanged. Commercial vehicles are to be freed completely from the 30 per cent tax formerly levied on vehicle chassis. The tax on TV replacement tubes is also eliminated. The reduction in sales taxes follows substantial changes made in last year's budget when the number of excise tax rates was reduced from 7 to 4 and goods then charged at the 90 and 50 per cent rates were reduced to 60 and 30 per cent, respectively.

Beer tax cut -- The cut in beer tax and liquor license duties is estimated to cost £36 million this fiscal year and £40 million in a full year. The effect of these reductions will be to reduce the price of beer to the consumer by 2 pence a pint, or some 10 per cent a glass.

Investment allowances -- A system of investment allowances, last in effect from 1954 to 1956, has been reintroduced. In essence, this system permits depreciation for tax purposes over the life of an investment to exceed 100 per cent. The new scheme will cost nothing in revenues this fiscal year but will rise to £9.5 million in 1960-61, and will vary thereafter depending on the volume of new investment. The new system modifies the first year accelerated depreciation allowances which were raised last year to 30 per cent for plant and machinery, and to 15 per cent for industrial buildings. Under the new system, first year accelerated depreciation allowances are reduced to 10 per cent on plant and machinery, 5 per cent on industrial buildings and 20 per cent on mining works. These are supplemented by a 20 per cent investment allowance or excess depreciation allowance for plant and machinery, 10 per cent for industrial buildings, and 20 per cent for mining works. The effect of these changes is to leave the first year's depreciation for these types of investment unchanged. However, an element of subsidy has been added to the extent that depreciation for tax purposes exceeds actual depreciation over the life of the investment.

Other cuts --- The Chancellor also made a number of other relatively minor changes in taxes. The license tax on commercial passenger vehicles was reduced in order to improve the competitive position of public transport enterprises. The uuremunerative and arbitrary Corporation Duty, introduced in 1885 to compensate the Treasury for loss of death duties on corporate held property, is abolished. The stamp duty on marine insurance policies (in effect a tax on exports) is also abolished at a cost of some £3 million in a full fiscal year. The amounts of remuneration directors of controlled companies can take out is raised by a moderate amount, at a cost of £3 million in a full year. In addition, certain oil taxes and taxes on life insurance policies for estate duty purposes are reduced.

Evaluation of the tax concessions

A rich man's budget? -- The income tax concessions, which give the greatest proportionate reduction in tax rates to those who pay taxes on taxable income below £360 annually, in fact grants more benefits to higher income groups who pay the bulk of the taxes. In 1957, 62 per cent of all income units had 84 per cent of all indentifiable personal incomes, above £400 annually, and paid 97.3 per cent of all personal income taxes and surtaxes. Putting it the other way, over 38 per cent of income units paid only 2.7 per cent of income and surtax in that year.

Table 3

Distribution of Personal Incomes and of Taxes Levied in 1957[a]

Range of income before tax	Number of incomes	Per cent of total	Income before tax (£ mill.)	Per cent of total	Income and surtax paid (£ mill.)
From £50 to £400	9,930	38.3	2,475	16.2	44
From £400 and over	15,970	61.7	12,775	83.8	1,571
	25,900	100.0	15,250	100.0	1,615

a/ These figures include taxable as well as nontaxable income. Income of persons receiving less than £50 a year is excluded. In 1957, £2,737 million of personal income could not be classified in the above ranges.

Source: National Income and Expenditure 1958, Central Statistical Office, H.M.S.O., London.

The tax reductions actually result in an increase in the progressive nature of Britain's tax structure in the sense that the percentage of income taken for taxes now rises more steeply from the lowest to the highest. This follows from the fact the lowest income groups received the largest percentage reduction. However, in terms of the amount of income retained after taxes the higher income groups, of course, receive greater benefits. For example, a single person with earned income of £250 a year will pay 27 shillings less tax than formerly, whereas a single person in the £1,000 bracket will pay 389 shillings less tax. Surtax payers who contribute 35 per cent of income taxes will receive £40 million, or 25 per cent, of the income tax concessions for a full year (£225 million).

Table 4

Income and Surtax of Single Person

(In shillings)

Taxable earned income (after standard deductions)	(a) Tax at old rates	(b) Tax at new rates	Difference (a) - (b)	Percentage reduction from (a) to (b)
5,000 (£250)	122	95	27	22.1
7,000 (£350)	478	411	67	14.1
12,000 (£600)	1,635	1,471	164	10.0
20,000 (£1,000)	4,221	3,832	389	9.2
120,000 (£6,000)	54,910	51,439	3,471	6.3
200,000 (£10,000)	113,185	106,500	6,685	5.9
Income and Surtax of Married Couples with Two Children not over 11				
12,000 (£600)	60	46	14	23.3
20,000 (£1,000)	1,710	1,541	169	9.2
120,000 (£6,000)	50,710	47,464	3,246	6.4
200,000 (£10,000)	108,385	102,467	5,918	5.5

Source: Derived from tax rate tables in Financial Statement (1959-60), House of Commons, April 7, 1959, London, H.M.S.O., pp. 23 and 26.

Stimulus to consumption -- The main direct stimulus to consumption is the across-the-board cut in sales taxes on most consumer durables. The ending of the credit squeeze and installment credit controls in the second half of 1958 was followed by a boom in credit sales of durable goods including autos. This buying was the principal expansionary influence in this period; it has accounted for a good part of the rise in bank loans since August 1958. The sales tax cuts will assist in maintaining the momentum of the consumer durables boom which many had feared would soon run out of steam.

The beer tax -- It has been suggested that the reduction in beer tax is the principal gesture towards those who pay little tax and can't afford many goods.1/ The Chancellor, in his budget speech, pointed out that a cut in this tax might help to prevent a further fall in beer consumption, and thereby in tax revenue on such consumption. He also added that the reduction in sales taxes and the beer tax "will make a useful contribution in keeping down the cost of living." The heavy weighting of beer in the cost-of-living index mainly accounts for the expected reduction in the index by four-fifths of a point.

Rises in Expenditure

Postwar credits -- During World War II extra taxes were levied in the form of compulsory noninterest bearing loans. These have been repaid mainly to the aged and heirs at the rate of some £18 million a year. The total outstanding now amounts to £430 million. The Government now intends to increase this repayment to £89 million this year or £71 million more than last year. This will be done by reducing the age at which people become eligible for repayment and by liberalizing hardship case provisions. Finally, the remaining credits will bear interest compounded annually at the rate of 2-1/2 per cent.

The accelerated repayment of these credits will amount to a corresponding increase in personal disposable income this fiscal year. The Chancellor may not be unduly optimistic in hoping that part of these funds will flow into national savings. Almost half of the repayment this year will go to people within several years of retirement who will presumably have a strong incentive to save. The other large remaining category will go to heirs of deceased holders of debt. Over 1.4 million people in addition to the existing 300,000 recipients are expected to benefit from these payments, which will average some £50 a person. The Chancellor has asked for statutory authority to vary the volume of postwar credit repayments by administrative order in the future.

Government investment outlays

Central Government capital outlays (largely loans and grants to nationalized industries, domestic housing and overseas Colonial and Commonwealth development) are expected to rise by £193 million this

1/ Economist, April 11, 1959, p. 147.

fiscal year. These changes in government capital outlays were in the main decided upon last fall. In September, direct British Government loan facilities for Colonial and Commonwealth governments were announced. In October 1958, the ceiling on public investment (imposed in September 1957) was lifted. At that time, it was announced that public investment in 1959-60 would be permitted to rise by £125 to £150 million above the 1957-58 level. In the April 1959 budget speech, the Chancellor announced that this level had since been raised to almost £200 million. Thus, in the last six months, over £75 million was added to -- largely short term -- public investment plans. Direct government and nationalized industries investment amounts to almost three-fifths of total public investment, the rest being provided by local authorities. The Government also exercises a measure of control over the timing, terms and character of other types of public investment.

Private investment is not expected to expand much in 1959. A forecast 10 per cent decline in manufacturing investment is expected to be offset by a rise in outlays in distributive industries and private housing. The authorities have accordingly decided to provide a strong impetus to the capital goods sector with an 11 per cent rise in public investment. Part of this investment is for coal mining modernization, railways, and electric power generation, and is necessarily long term in nature. Programs, such as expanded local authorities' housing projects, can be reversed relatively quickly as in the past. Since the public investment sector accounts for close to 45 per cent of gross fixed capital formation in the United Kingdom, a rise of 11 per cent means that the authorities expect total gross fixed capital formation to rise by some 5 per cent this year.

General observation and evaluation

The sizable tax concessions granted and increased public investment contemplated are prompted by the disappointingly slow rate of recovery from the 1958 recession. The Government believes that there is a sufficient margin of unused resources at home to warrant the expansionary budget, despite the extensive fiscal and monetary measures already taken, and that the strong balance-of-payments position makes such easing possible.

Table 5

British Budget

Capital or below-the-line Net Outlays

(In millions of pounds)

	1958-59 outcome	Net change	1959-60 estimated
Net loans to nationalized industries:			
Coal Board	88	+ 2	90
Transport	323	+120	443
Other nationalized	94	- 6	88
Total nationalized industry	505	+116	621
Housing outlays and loans	25	+ 28	53
Post Office capital	33	- 2	31
Export credit guarantee loans (Commonwealth)	14	+ 29	43
Colonial loans	6	+ 24	30
Local authority repayments	(52)	- 3	(55)
Other	10	+ 1	11
	541	193	734
Postwar credits	18	+ 71	89
Net capital deficit	559	+264	823

Source: Derived from Financial Statement 1959-60, House of Commons, April 7, 1959, London, H.M.S.O.

The measures, taken to expand activity in the second half of 1958, have not apparently had the desired effect on internal activity.[1/] Industrial production, seasonally adjusted, rose from 105 in the third quarter of 1958 to 107 in November where it has remained since. Unemployment in March was only 2.4 per cent of the labor force but is high by postwar British standards. hile there are signs that the decline in the rate of inventory accumulation may have ended in the fourth quarter of 1958, there has been little revival in capital goods industries. Private investment is expected to show only a small rise this year. The major factor sustaining recovery so far has been the boom in installment credit sales of consumer durables.

The authorities believe that a substantial margin exists for further expansion. Not only are the effects of the recession to be overcome, but much unused capacity was created in the years of high investment from 1955 through 1957. However, one recent report suggests that excess capacity is unevenly spread and that in some fields changes in market conditions may have created permanent redundancy.[2/] The policy of official restraint imposed in September 1957, coupled with the subsequent reduction in internal demand, led to a moderation of the chronic postwar price wage spiral; the cost of living rose by only 2 per cent in 1958 and wages by 3.5 per cent.

The external position is also stronger than it has been for some years. British reserves in 1958 rose by £274 million (they are now £1,158 million) while her sterling liabilities increased by only £76 million. The principal factor contributing to the record £455 million balance-of-payments surplus in 1958 was the 10 per cent fall in import prices at a time when reduced foreign demand led to a 3-1/2 per cent fall in exports. In part, the demand for imports was limited by falling prices and to a slowdown in the rate of inventory accumulation. With imports rising again, the trade deficit in the first quarter of

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1/ In July 1958, the credit squeeze came officially to an end; the ceiling on bank loans was abolished and control of new capital issues was liberalized. The banks with official sanction, entered the field of hire-purchase finance and greatly expanded their personal loan facilities. Installment credit controls were relaxed in September 1958 and then abolished six weeks later. The ceiling on public investmentment was removed in October and local authorities were encouraged to undertake capital projects. In November, a program of direct Treasury loans for house purchases was announced. Earlier at the Commonwealth conference a system of direct Treasury loans to Commonwealth and colonial governments was announced. In February 1959, Capital Issues Controls for all private domestic borrowers were suspended.

2/ "An Industrial Journey, Recession and Recovery," by the Financial Editor of the Manchester Guardian, Reprint, March 1959.

1959 was £119 million compared to £76 million a year earlier. The recent strength of the pound is attributable to expanded British exports to the U.S., Canada and a number of European countries and to the recovery of sterling area primary product exports to nonsterling areas.

Last year, the authorities were able to make substantial security sales to the market and to small savers. Long-term interest rates were maintained at a high level throughout the year as the authorities fed bonds into the market to cushion price rises. Since the fall of 1957, for example, short-term rates declined by over 3 per cent but long-term rates by only one-half of one per cent. Sales of small savers securities (nonmarketable) rose during 1958 following the higher rates and more liberal terms announced in last year's budget; these favorable terms were not altered despite the decline in interest rates last year.

Because the Treasury used cash obtained from bond sales to reduce debt held by the banking system, the banks were able to expand advances appreciably without any expansion in bank deposits. Between July 1958 and April 1959, bank deposits were almost unchanged; yet bank advances rose £511 million (25 per cent), which the banks financed by sales of £309 million of bonds and £268 million of Treasury bills.

The Government's recovery program to date has relied mainly on expansionary fiscal and monetary actions. Yet the experience of the 1955-57 private investment boom clearly showed the need for both fiscal and debt-management support for a program of monetary restraint in Britain. The public sector is such a large part of the British economy, and the annual maturities of public debt are so great that these two areas of fiscal management can frustrate attempts to use monetary policy as a principal instrument of economic stabilization. The primary concern about the new budget rests fundamentally on whether fiscal restraints can be applied as recovery proceeds: the heavy tax cuts and increased public investment outlays contemplated mean that the Treasury will need more new money from the capital market than it has sought in recent years. The heavy cash needs together with the rolling over of maturing debt, will have to come predominantly from outside the banking system (as funds were obtained in 1958-59) if the effectiveness of monetary policy is not once again to be blunted by Treasury financing needs.