

Spending Review 2004

The current government has repeatedly promised to cut public sector administration costs and halt the rise in civil service jobs, yet both have risen year after year. Gordon Brown promised to try again in today's Spending Review - and with polling day perhaps just 10 months away he needs to convince the voters not only that this can be delivered but that it can be done without hurting public services.

Mr Brown's latest proposed economies are certainly eye-catching. He trumpeted plans to axe more than 70,000 Whitehall civil servants over four years, although 40,000 of these were announced in the Budget and 15,000 of them had in turn also been in earlier Treasury plans. Up to 20,000 more could go from local, Welsh and Scottish government.

If achieved this would more than reverse the increase in civil service numbers from around 500,000 to 550,000 that we have seen since the government took the brakes off public spending in 1999-2000.

But civil service numbers have exceeded Treasury plans in every set of annual public spending projections since 1999. For example, if the plans published by the Treasury in May 2002 had actually been achieved, there would already be about 45,000 fewer civil servants than there are now.

Today the Treasury also pledged a cut in administration costs across Whitehall of 6% a year in real terms. This would reduce the cost of bureaucracy from 3.1% of total spending in 2005-06 to 2.8% in 2007-08 and save around £2bn.

Comparing planned bureaucracy with past performance is complicated as the Treasury has cut its forecast for administration costs in 2005-06 by almost a quarter by reclassifying £5bn of administration costs in the Home Office and other legal departments as "frontline" spending. But, prior to the reclassification, the Treasury had promised every year since 1998 to reduce administration spending, only to see it rise consistently.

Hard though they are to deliver, cuts in civil service and administration costs are only part of the economies the chancellor is looking for. He reiterated his Budget target of delivering efficiency savings of more than 2.5% each year across the whole public sector, saving more than £20bn by 2007-08 to be ploughed back into front-line public service delivery.

No-one will need convincing that the public sector could be run more efficiently, but whether and for how long it would be possible to produce 2.5% more each year for the same money is hard to know. This is slightly more than the private sector typically achieves, but rather less than was squeezed out of many public enterprises when they were privatised.

Public sector efficiency at this broad level is hard even to measure, let alone to improve. It is very difficult to identify the quantity and quality of the outputs that some public services produce. What, for example, is the measurable "output" of the armed services? And would we know if we were getting 2.5% more of it for every pound spent in a year's time?

The Treasury is well aware of these difficulties. It set itself the target of delivering 2.5% efficiency savings in the 1998 Comprehensive Spending Review, only for its officials to have to admit to MPs last year that “it has not been possible to measure efficiency for the whole of the Treasury in quite those terms... This would be extremely difficult to do given that the activities the Treasury has been engaged in have changed.”

Mr Brown’s search for efficiency savings has been driven by the fact that this has necessarily been a much tighter review than those that have preceded it. The big rise in spending we have seen since 1999-2000 has been financed largely through borrowing. So, to shrink the deficit and adhere to his self-imposed fiscal rules, the chancellor is already relying on an increase in the tax burden and – after the next election – slower spending growth.

Mr Brown confirmed that, after growing by 4.2% on top of inflation in 2005-06 (presumably election year), total spending will rise by an average of just 2.7% a year in real terms in 2006-07 and 2007-08.

Over these two years, departmental spending is planned to rise by 3.4% a year in real terms and “annually managed expenditure” (on things like social security benefits and debt interest) by 1.8%.

Almost every department will receive smaller real increases in 2006-07 and 2007-08 than over the last Spending Review period, suggesting that the pain has been relatively widely spread. Most will see their budgets shrink as a share of national income.

The biggest losers relative to the last Spending Review include the Department of Trade and Industry, the Office of the Deputy Prime Minister and the Department for the Environment, Food and Rural Affairs. Taking one-off spending projects into account, transport also did less well than many commentators might have expected.

Mr Brown wasted no opportunity during his speech to contrast his plans with those of the Conservatives. They intend to match his pledges on health and education but squeeze budgets more tightly elsewhere to reduce spending as a share of national income and thus limit the extent to which the tax burden needs to rise.

Both parties are constrained in what they can promise on tax and spending by the public finances. Hence their reliance on efficiency gains to square the circle. Mr Brown must hope that the substantial savings he promised today are modest enough to be believable, but not so modest that the voters think the Conservatives can do better.

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Notes to Editors:

1. A briefing will be held at IFS at 12.30 on Tuesday 13th July. Please contact Bonnie Brimstone at bonnie_b@ifs.org.uk if you would like come.