Public spending: more cuts to come

Carl Emmerson


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Tax rises and spending cuts to eliminate the deficit

- March 2015 Budget
- Conservatives

% of national income

Financial year

Notes and sources: see Figures 3.1 and 4.1 of Post-election Austerity: Parties’ Plans Compared.
Manifesto commitments on total spending

- **March 2015 Budget**
- **Conservatives**

<table>
<thead>
<tr>
<th>Financial year</th>
<th>£ billion, 2015–16 prices</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007–08</td>
<td>660</td>
</tr>
<tr>
<td>2008–09</td>
<td>680</td>
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<tr>
<td>2009–10</td>
<td>700</td>
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<td>2010–11</td>
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<td>2016–17</td>
<td>840</td>
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<td>2017–18</td>
<td>860</td>
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<tr>
<td>2018–19</td>
<td>880</td>
</tr>
<tr>
<td>2019–20</td>
<td>900</td>
</tr>
</tbody>
</table>

Notes and sources: see Figure 4.1 of Post-election Austerity: Parties’ Plans Compared.
Underlying pressures pushing spending up

- Components of Annually Managed Expenditure forecast to rise:
  - debt interest: increased government debt and rising effective interest rate
  - public service pensions: numbers receiving rising
  - state pensions: average payments rising
- Given cut to overall spending implies a deeper cut to departmental spending
- Decision to increase some spending, and not to cut some other spending, increases the size of the cuts faced elsewhere
Manifesto commitments on social security spending

• Pledged £11.1bn (today’s terms) of cuts to annual social security by 2017–18 (£12bn nominal in 2017–18)
  – £220bn of spending, but £95bn on state pension and universal pensioner benefits protected
  – so unprotected spending to be cut by about 10% which would reduce it to lowest level as a share of national income since 1990–91

• Announced measures achieve one-tenth of this:
  – £1.0bn: freeze most working-age benefits in 16–17 and 17–18
  – £0.1bn: reduce benefits cap from £26k to £23k
  – £0.1bn: remove housing benefit from 18-21 yr-old JSA claimants

• Leaves about £10bn more cuts to find in 2 years
  – via policies other than ‘just’ increasing things less quickly than inflation
  – over last 5 years, excluding policies to increase benefits less quickly than inflation, coalition found £15bn of gross cuts
What could be cut? (some illustrative examples)

Unprotected benefit spending: £125 billion in 2015–16

- **£5bn**: reducing child element of child tax credit / universal credit by 30% (back to its real 2003–04 level)
- **£2½bn**: making all housing benefit recipients pay at least 10% of their rent
- **£1½bn**: Taxing universal disability benefits

Departmental cuts: the story so far

- Average real cuts of 9.7% between 2010–11 and 2015–16
  - less than was planned over the four years to 2014–15 in SR2010
  - despite cash day-to-day budgets being cut back further
  - due to lower-than-forecast inflation and capital spending being topped up

- Cuts over this period far from evenly spread
  - increases in spending on overseas aid, relative protection from cuts for the NHS and day-to-day schools spending
  - cuts of 25% or more to some unprotected departments including Home Office, Ministry of Justice, Communities & Local Government and Business, Innovation & Skills
Three more years of departmental spending cuts

2007–08
2008–09
2009–10
2010–11
2011–12
2012–13
2013–14
2014–15
2015–16
2016–17
2017–18
2018–19
2019–20

£ billion, 2015–16 prices

Outturns

Conservatives (with £12bn of social security cuts by 2017–18)

Spend in 2018–19 6.6% lower than in 2015–16 (real cut of £23.8 billion)

Spend in 2018–19 15.6% lower than in 2010–11 (real cut of £62.8 billion)

2.0% per year average cut

2.2% average cut

Notes and sources: see Figure 6.1 of Post-election Austerity: Parties’ Plans Compared.
Departmental cuts: the next chapter?

• Conservative manifesto pledged to protect 3 areas of spending:
  – aid: continue spending 0.7% national income on ODA
  – schools: protect cash spending per pupil
  – health: spend at least an additional £8 billion (real terms) by 2020

• Together imply additional real terms spending of £6.2 billion between 2015–16 and 2018–19
  – requires cuts elsewhere to amount to £30.0 billion or 15.3%
  – cumulative cut to unprotected departments since 2010–11 would reach 32.9%
  – freezing defence spending through to 2018–19 would increase the cuts required elsewhere to 18.7% (or 36.9% since 2010–11)

• Block grant to Scotland to fall, but by less than 6.6%
Reducing the public sector wage bill

• General government employment
  – reduced by 376,000 between 2010Q1 and 2014Q4, fall of 80,000 in 2015–16 forecast by the OBR
  – now down to the level of the early 2000s and to the lowest share of workforce since at least early 1970s

• Public sector pay also squeezed
  – our estimates suggest all of the increase in the estimated public sector pay differential seen since the financial crisis began now unwound

• Difficult trade-off between 2015–16 and 2018–19
  – if public sector pay increases in line with OBR projection then we estimate a further 500,000 reduction in general government employment
  – this would reduce it to its lowest level since 1974
  – CPI indexation of pay through to 2018–19 would still require a further 350,000 reduction in general government employment

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Will the cuts be delivered?

• Coalition government successful in keeping (broadly) to the spending plans set out in 2010
• But reasons to think cuts likely to be harder this parliament
  – squeezing public sector pay will get harder as private wages increase
  – efficiencies easiest to identify and deliver presumably have been made
  – programmes judged to be low-value presumably already scrapped
  – ending of contracting out increases NICs bill of public sector employers (£3.3bn)
  – latest pension scheme valuations push up the required employer contribution rate (£1.1bn)
  – new commitments: extension of free childcare (£350m); new tax-free childcare (£0.8bn); abolition of cap on HE student numbers (£0.7bn); Dilnot social care (£1.0bn)
  – population continues to grow (and age)
Conclusions

- Manifesto commitment to cut spending through to 2018–19
  - eliminate the deficit without announcing significant net tax rises
- Underlying pressures pushing up spending in some areas
- Even with £12bn of social security cuts pace of departmental spending cuts set to accelerate slightly
  - further 6.6% to come from departments over next three years, bringing cumulative cut since 2010–11 to 15.6%
- NHS and overseas aid spending to rise, cash schools spending per pupil protected from cuts
  - spending on unprotected departments set to be cut by a further 15.3%, bringing cumulative cut to these departments to 32.9%
  - freezing defence spending would increase this cumulative to cut to 18.7%, or 36.9% since 2010–11
- Meeting these spending plans will not be easy
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