Background to the 2010 Spending Review

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The Chancellor will present the Spending Review to the House on 20 October. This will set out the Government's spending plans for the next four years. It is expected to announce very sharp reductions in the budgets of most government departments.

A debate in the House of Commons will take place on Thursday 28 October.

This note gives the background to the Spending Review. A separate note gives details of the Spending Review announcement and the reaction to it.

Update: 19 October

Some further details about the Spending Review have been reported in the press since this note was published on 15 October. These include:

- An increase in the schools budget in England, although this appears to include the pupil premium announced by the Deputy Prime Minister on 15 October.

- Confirmation of a number of capital spending projects, including Crossrail, the Mersey Gateway Road Bridge and the Synchotron in Oxfordshire

In addition, the Prime Minister announced on 19 October that the defence budget will be cut by 8% in real terms over four years.

The Shadow Chancellor, Alan Johnson, gave a speech on 18 October in which he reaffirmed Labour's policy to halve the deficit by 2013/14. He also said that targeted tax changes needed to play a greater role in reducing the deficit and that the banks should make a greater contribution.

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1 Summary

The Chancellor will deliver his statement on the 2010 Spending Review to the House on Wednesday 20 October providing further detail on the Government's spending plans.[1] These are expected to include sharp reductions in the budgets of many government departments. The Spending Review will also be debated in the House on Thursday 28 October.

The Government's top priority is reducing the budget deficit which was £156 billion in 2009/10. The Budget set out plans to cut the deficit, announcing £32 billion of spending cuts by 2014/15. These are in addition to the reductions in spending which had been planned by Labour. Public spending is forecast to fall in real terms for each of the next four years. This is a very sharp reduction: since 1970, spending has fallen in real terms in only five years and only once for two consecutive years (1996/97-1997/98). Despite these cuts, public spending as a share of the economy in 2015/16 will still be higher than it was in 2003/04.

The Government has pledged to protect health spending and the overseas aid budget. Health spending will rise in real terms in every year of this Parliament and the Government is committed to the target of overseas aid spending reaching 0.7% of national income by 2013. As the health budget is the largest among Whitehall departments, protecting it will mean the cuts to other departments' budgets will be deeper. The Treasury has said that unprotected departments may face average real terms cuts of 25% over the four years of the Spending Review. As this is an average figure, some departments are likely to face even greater cuts. Press reports indicate that most departments have been asked to outline to the Treasury how they could make cuts of up to 40%. Departmental cuts could be reduced if greater savings can be made from the welfare budget. For example, the Government recently announced changes to child benefit which it claims will save £1 billion a year by 2013.

The Spending Review raises a number of key issues, including its effect on the economy and public services and the fairness of the cuts. On the economy, the Government argues that reducing the deficit is necessary for the economic recovery. Failure to cut the deficit would risk higher interest rates and loss of confidence. The Opposition argues that the Government's policies pose risks to the recovery which remains fragile.

The Government has said that "it will look closely at the effects of its decisions on different groups in society, especially the least well off, and on different regions".[2] Some countries and regions of the UK, such as Scotland, Wales, Northern Ireland and the North of England, are relatively dependent on the public sector for employment and have higher levels of public spending per head, suggesting that they may be more at risk from the cuts. The Government has announced a number of policies to help the regions such as the Regional Growth Fund and cuts in national insurance for new businesses.

Fairness can, however, be interpreted in different ways, as the recent announcement on child benefit demonstrates. The Government argues that it is unfair for lower income families to pay for child benefit for the rich. The Opposition points to the fact that households with the same income will be treated differently for child benefit purposes, depending on whether they contain a higher rate taxpayer.

[1] The date of the Spending Review was announced by the Chancellor in his Budget statement (HC Deb 22 June 2010 c171)

[2] HM Treasury, *The Spending Review framework*, June 2010, Cm 7872, para 2.4

2 What are Spending Reviews?

The system of spending reviews was introduced under the last government to set departmental spending limits for a number of years ahead. Spending Reviews were held in 1998, 2000, 2002, 2004 and 2007. The Labour Government did not hold a Spending Review after 2007 because of the uncertain economic outlook.[3]

Public spending is divided between DEL (Departmental Expenditure Limits) and AME (Annually Managed Expenditure). DEL refers to departmental expenditure which can be planned for several years ahead. It includes administration costs and most programme expenditure. In 2009/10, DEL amounted to £379 billion (57% of total public spending). Health, education and defence have the largest DELs (see chart below). The devolved administrations also have significant budgets. Spending on devolved functions, such as education and health, is financed from these budgets.

Departmental Expenditure Limits, 2010/11
£ billion

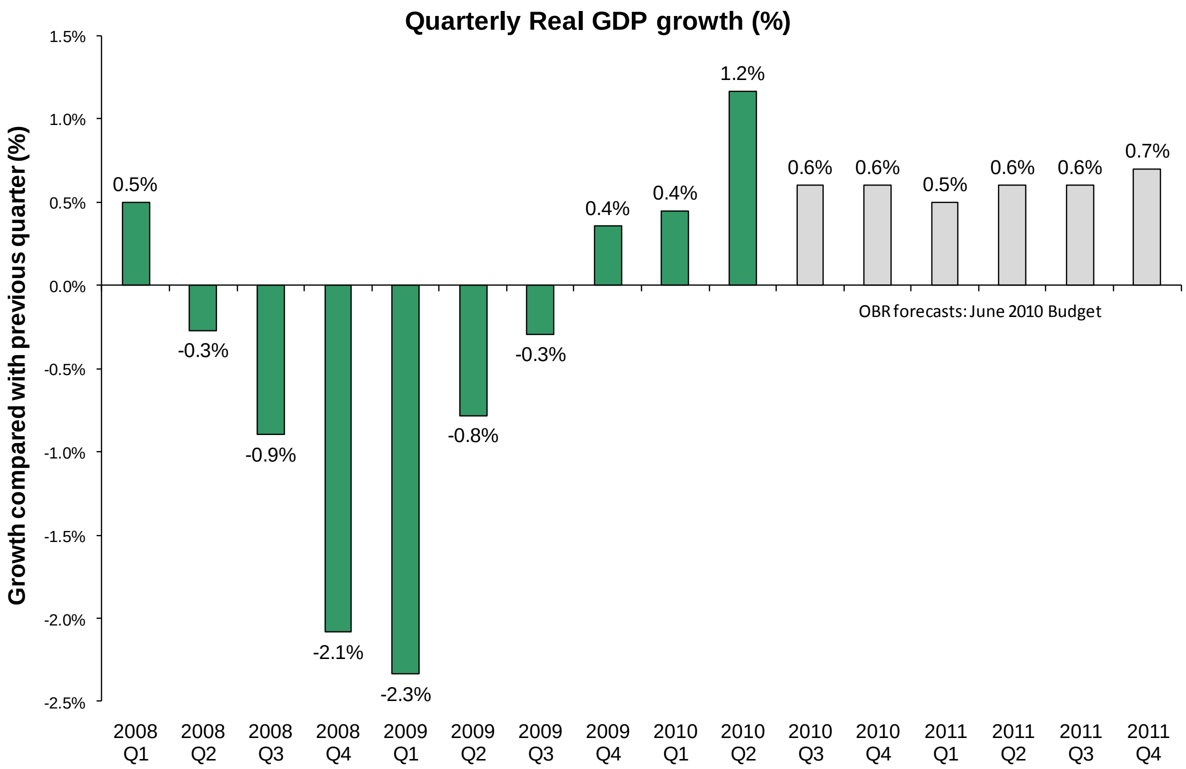
[3] HC Deb 16 March 2010 c757W

AME refers to Annually Managed Expenditure. This spending is more difficult to predict and plan several years ahead. The main element of AME is social security benefits and tax credits. Debt interest is also included in AME. In 2009/10, AME was £291 billion (43% of total public spending).

3 The economic background

3.1 The economy

The economy has grown for three successive quarters since the recession. The latest data show (a generally unexpected) increase in quarterly GDP of 1.2% in 2010 Q2, the largest quarterly rise in GDP since the third quarter of 1999. The recent path of economic growth is shown in the chart below:



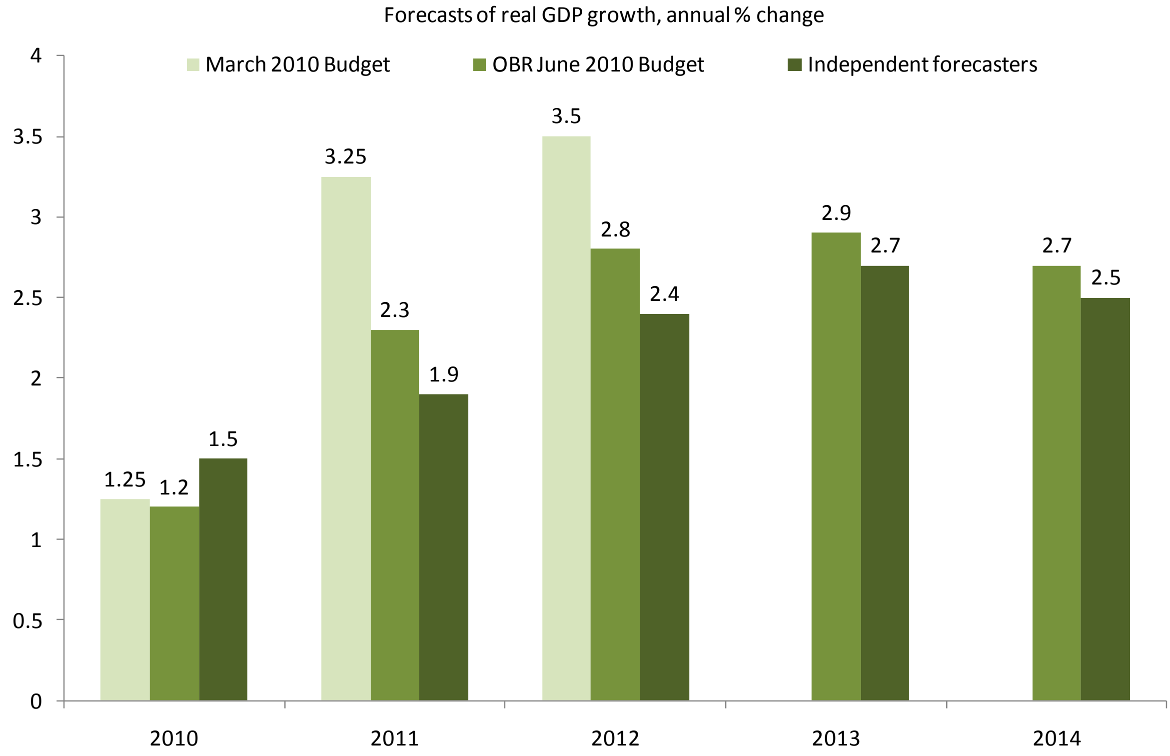
The June 2010 Budget contained economic forecasts from the new Office for Budget Responsibility (OBR). The OBR forecast growth in 2010 of 1.2%. It was more optimistic for 2011 and 2012 with forecasts of 2.3% and 2.8% respectively. The June 2010 Budget stated:[4]

> GDP growth rises from 2010, reaching 2.9 per cent in 2013. Growth then eases in 2014 and 2015, as demographic changes reduce the growth of the potential labour supply, though actual growth remains above trend.
>
> In the near term, economic activity is weaker than in the pre-Budget forecast. On the demand side this reflects Budget measures which restrain government spending and real household disposable income, holding back consumer demand. In 2010 as a whole GDP is forecast to rise by 1.2 per cent followed by 2.3 per cent in 2011 (against 1.3 per cent and 2.6 per cent in the pre-Budget forecast). From 2012 onwards GDP growth recovers as prices and wages adjust and monetary policy continues to support demand. Compared with the pre-Budget forecast, growth is stronger from 2013

[4] HM Treasury, Budget 2010, HC 61, June 2010 paras C.17-18

onwards as the economy adjusts back towards potential output. By the end of the forecast the adjustment is still not quite complete, so that the output gap is slightly larger in 2014 than it was in the pre-Budget forecast

The chart below compares the Treasury's March 2010 Budget forecasts with the OBR's June 2010 Budget forecasts and the average of independent forecasters[5]:



Forecasts by the IMF show that the UK economy is expected to grow by 1.7% in 2010, the lower than four other members of the G7 (see table below).

International comparisons of real GDP growth

% change

	2009	2010	2011
Canada	-2.5	3.1	2.7
France	-2.5	1.6	1.6
Germany	-4.7	3.3	2.0
Italy	-5.0	1.0	1.0
Japan	-5.2	2.8	1.5
UK	-4.9	1.7	2.0
US	-2.6	2.6	2.3
Euro area	-4.1	1.7	1.5

Source: IMF World Economic Outlook, October 2010, Table A2

[5] The independent forecasts for 2010 and 2011 are from the September edition of the Treasury's *Forecasts for the UK economy*. The forecasts for 2012 - 2014 are from the May edition.

These forecasts all suggest that the UK economy will grow (albeit at a relatively slow pace) over the next few years. While there are a number of factors which should work to boost the economy - interest rates remain at historically low levels and sterling has declined by 23% since its peak in July 2007, which should provide a boost to exporters - other factors suggest the UK economy is still not free from the spectre of a 'double-dip' recession. Business confidence in the private sector, especially amongst companies that are reliant on public sector contracts, is low. Although business investment has risen during the first half of 2010 it still remains below its pre-recession high (2007) as businesses build cash reserves in expectation of lower future revenues. Lending by banks to businesses is still difficult to access and less affordable for many businesses since the credit crunch. Unless growth in the private sector balances the anticipated fall in public sector expenditure over the next few years, the outlook for the UK economy will remain uncertain.

Further detail on the economy is available in the Library's *Economic Indicators* Research Paper.

3.2 The public finances

The Government has said that reducing the deficit is "the most urgent task facing this country".[6] In 2009/10, the budget deficit was £156 billion (11% of GDP). The UK's budget deficit is among the highest of the G7 economies (see table below).

International comparisons of government deficit — % GDP

	2009	2010	2011	2015
Canada	5.5	4.9	2.9	0.2
France	7.6	8.0	6.0	2.2
Germany	3.1	4.5	3.7	1.4
Italy	5.2	5.1	4.3	3.0
Japan	10.2	9.6	8.9	7.4
UK	10.3	10.2	8.1	2.4
US	12.9	11.1	9.7	6.5
Euro area	6.3	6.5	5.1	2.8

Source: IMF World Economic Outlook, October 2010, Table A8
Note: figures are compiled on a different basis than the ONS and Treasury figures for the UK. They are for calendar rather than financial years.

The June Budget set out plans to reduce the deficit to £20 billion or 1.1% of GDP by 2015/16.[7] The majority of the fiscal consolidation comes through reductions in public spending rather than tax increases. As the table below shows, by 2014/15, £83 billion of the £113 billion fiscal tightening (74%) comes through spending cuts. The previous Government had planned to cut the deficit more slowly. In its March Budget, Labour had set out plans to more than halve borrowing over four years (to £74 billion or 4.0% of GDP) by 2014/15. According to the June Budget, £73 billion of the £113 billion planned consolidation (65%) was planned by the previous Government, including £52 billion spending cuts.

6 HM Treasury, *Budget 2010*, June 2010, p1
7 HM Treasury, *Budget 2010*, June 2010, Table C6, p89, Table C7, p90

Fiscal consolidation plans *£ billion*

	2010/11	2011/12	2012/13	2013/14	2014/15
Discretionary policy announced in June 2010 Budget					
Total	8.1	15	24	32	40
Spending	5.2	9	17	24	32
Tax	2.8	6	7	9	8
Policy inherited by the Goverment					
Total	0.8	26	42	57	73
Spending	0	14	25	39	52
Tax	0.8	11	17	18	21
Total discretionary consolidation					
Total	8.9	41	66	90	113
Spending	5.2	23	42	63	83
Tax	3.6	18	24	27	29

Source: HM Treasury, June 2010 Budget Table 1.1

The Government argues that rapid action to cut the deficit is necessary for economic recovery. Unless the deficit is cut quickly, there is a risk that higher interest rates and loss of confidence could harm the recovery. In addition, the Government argues that:

- Higher levels of debt mean higher debt repayments reducing the resources which can be devoted to public spending priorities.
- Debt can rise rapidly during recessions. High levels of debt reduce the government's ability to respond to future downturns.
- Borrowing is only deferred taxation: it would be irresponsible to accumulate substantial debts which would need to be paid off by future generations.[8]

The Opposition argues that sharp spending cuts risk undermining the fragile economic recovery and that the cuts will hit the poorest in society.

In its recent report on the UK economy, the IMF said:

> The UK economy is on the mend. Economic recovery is underway, unemployment has stabilized, and financial sector health has improved. The government's strong and credible multi-year fiscal deficit reduction plan is essential to ensure debt sustainability. The plan greatly reduces the risk of a costly loss of confidence in public finances and supports a balanced recovery. Fiscal tightening will dampen short-term growth but not stop it as other sectors of the economy emerge as drivers of recovery, supported by continued monetary stimulus.[9]

On the Government's approach to fiscal policy, the IMF commented as follows:

> The government's strong deficit reduction plan will ensure fiscal sustainability. The fiscal mandate of balancing the cyclically-adjusted current budget by 2015/16 is

[8] HM Treasury, *The Spending Review framework*, June 2010, Cm 7872, para 1.2

[9] IMF, *Article 4 Statement on the UK economy*, 27 September 2010

appropriately ambitious. The plan's credibility has been bolstered by a frontloaded path that achieves the mandate one year early and by a suitable mix of concrete spending and revenue measures. The consolidation plan and implementation of early measures to tackle the deficit—one of the highest in the world in 2010—greatly reduces the risk of a costly loss of confidence in fiscal sustainability and will help rebalance the economy. These benefits outweigh the expected costs in terms of adverse effects on near-term growth. Indeed, market reaction to the adjustment plan has been positive. Nonetheless, the magnitude of the growth headwinds from fiscal adjustment is uncertain and could be different than anticipated. In this case, the free operation of automatic stabilizers in both directions, alongside further support from monetary policy, provides an important safeguard even as structural consolidation continues.[10]

Others have argued that the Government's approach is misguided. For example, Martin Wolf, the chief economics commentator of the *Financial Times,* has argued that it is probable that the Government's plans will generate a recession.[11]

4 What has the Government announced so far?

4.1 Guiding principles

In June, the Government published *The Spending Review framework*.[12] This set out the following criteria for ensuring value for money:

- Is the activity essential to meet Government priorities?
- Does the Government need to fund this activity?
- Does the activity provide substantial economic value?
- Can the activity be targeted to those most in need?
- How can the activity be provided at lower cost?
- How can the activity be provided more effectively?
- Can the activity be provided by a non-state provider or by citizens, wholly or in partnership?
- Can non-state providers be paid to carry out the activity according to the results they achieve?
- Can local bodies as opposed to central government provide the activity?[13]

The framework document also said:

In light of its commitments to fairness and social mobility, the Government will look closely at the effects of its decisions on different groups in society, especially the least well off, and on different regions. Coupled with the radical reforms the Government has proposed for welfare, taxes and education, this Spending Review will make supporting those most in need a priority.[14]

In a speech in August, the Chancellor said:

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10 *Ibid.*
11 "Why the Balls critique is correct", *Financial Times*, 3 September 2010
12 HM Treasury, *The Spending Review framework*, June 2010, Cm 7872
13 HM Treasury, *The Spending Review framework*, June 2010, Cm 7872, para 2.5
14 HM Treasury, *The Spending Review framework*, June 2010, Cm 7872, para 2.4

Difficult choices will have to be made.

Not just to make the sums add up - but so that this Spending Review is about more than making those sums add up.

As we take decisions that will affect the budgets of government departments and public services for years to come, we have to make sure that:

- We are shaping the economy of the future by promoting a pro-growth agenda;
- That we are shaping the big society of the future by decentralising power and empowering people;
- That we are shaping the public services of the future by reforming the public sector so it delivers value for money;
- That we are shaping Britain's future role in the world through our review of defence and security.

It is not about how much the Government spends but about what the Government actually does with the money.

We want to be laying the future foundations for economic growth and for a fairer society.

Fairness and growth. Two guiding principles we will apply to the decisions Britain has to take.[15]

4.2 The Spending Review process

The Government has formed a Committee of senior cabinet ministers to advise the Cabinet on the Spending Review. This Committee, the Public Expenditure Committee (PEX), often referred to as the "Star Chamber", initially had the following membership:

- George Osborne, Chancellor of the Exchequer (Chair)
- Danny Alexander, Chief Secretary to the Treasury
- William Hague, Foreign Secretary
- Francis Maude, Minister for the Cabinet Office and Paymaster General
- Oliver Letwin, Minister of State at the Cabinet Office.

Other members of the Cabinet may be added once their department has reached its spending review settlement with the Treasury. Press reports indicate that Eric Pickles (Communities and Local Government), Chris Huhne (Energy and Climate Change) and Caroline Spelman (Environment, Food and Rural Affairs) have reached agreement with the Treasury over their spending plans and have joined the "Star Chamber".[16]

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15 Speech by Chancellor of the Exchequer at Bloomberg, 17 August 2010

16 "Whitehall under the axe", *Guardian*, 2 October 2010; "Huhne agrees four-year energy funding settlement", *Guardian*, 1 October 2010

The Committee began weekly meetings at the end of August.[17] In a statement to the House of Commons on 13 September, the Chancellor said that the Committee had already met twice in September and would meet again that week.[18]

In August, Sir Philip Green was appointed to assist the Government in finding savings. Sir Philip's report was published on 11 October.[19] It focused on procurement and management of the government's property. The report found that the government failed to exploit its scale, buying power and credit rating and that the lack of a centralised approach meant that different departments were paying very different amounts for the same item.[20] While the report did not quantify the savings, the government spends £191 billion on procurement and property, so a 5% reduction would save nearly £10 billion.

The Government also launched a "Spending Challenge" through which public sector workers and members of the public could contribute ideas.[21] Some of these ideas have been taken up by the Government.[22]

4.3 Overall spending totals

The June Budget set the planned overall level of public spending for the period to 2015/16. The spending to be allocated by the Spending Review (sometimes referred to as the "envelope") is shown in the table below.

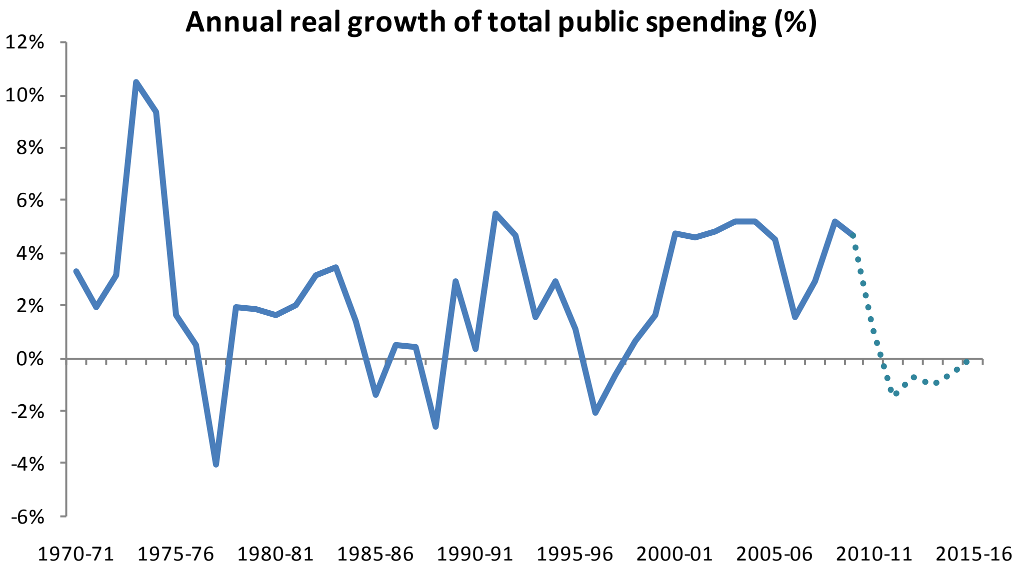
Spending envelope for Spending Review 2010 *£ billion*

		2011/12	2012/13	2013/14	2014/15
Total spending envelope		639.6	644.7	649.3	658.7
Of which:	Resource	591.6	598.9	606.7	614.5
	Capital	48.0	45.8	42.6	44.1
Total Public Expenditure		699.8	711.0	722.0	737.5

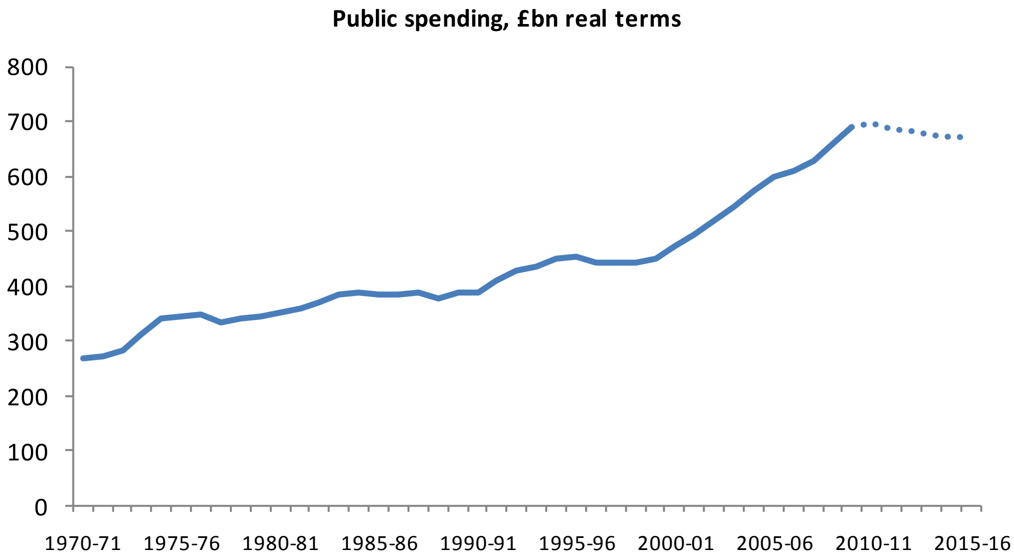
Source: HM Treasury, June 2010 Budget, Table 2.3
Note: SR envelope excludes central government debt interest, BBC domestic services, National Lottery and net expenditure transfers to EU institutions as these are either self-financing or not directly within Government control

The Budget forecast shows the scale of the cuts in total public spending. Total spending is forecast to grow by 1.2% in 2010/11, followed by four consecutive years when spending falls in real terms (see chart below). Since 1970, public spending has never fallen in real terms for more than two consecutive years (as happened in 1996/97 and 1997/98).

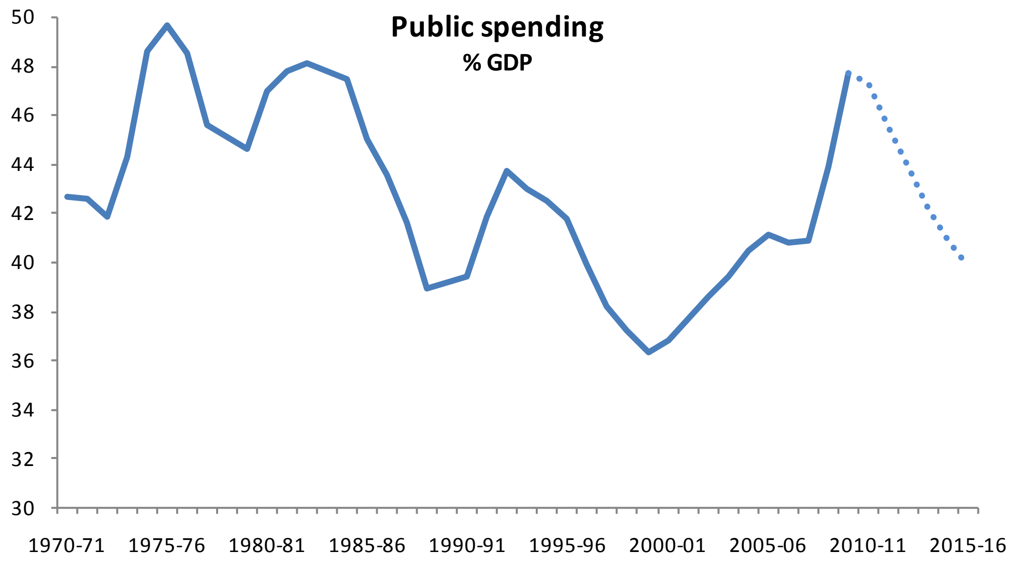
17 Speech by Chancellor of the Exchequer at Bloomberg, 17 August 2010
18 HC Deb 13 September 2010 c600
19 *Efficiency Review* by Sir Philip Green, Cabinet Office, 11 October 2010
20 Cabinet Office Press Release, *Sir Philip Green reports findings of his review into Government efficiency* , 11 October 2010
21 http://spendingchallenge.hm-treasury.gov.uk/
22 HM Treasury Press Release, *Government implements saving ideas submitted through the Spending Challenge*, 10 September 2010



The level of public spending in real terms (2010/11 prices) is show in the chart below. While public spending falls in real terms in each of the next four years, its forecast level in 2015/16 is still above that of 2008/09 but lower than in 2009/10.



Public spending is forecast to fall sharply as a share of GDP over the coming years: to 39.8% by 2015/16 from a peak of 47.7% in 2009/10. This is a fall of 7.9 percentage points over a six year period. While this is a sharp contraction compared with recent years when spending has grown faster than the economy as a whole, it is similar to decreases seen in the past. For example, in the mid-1990s public spending fell by 7.4 percentage points over seven years and in the 1980s it fell by 9.2 percentage points over a six year period. The level of public spending forecast for 2015/16, as a share of GDP, is still higher than it was between 1997/98 and 2003/04.



4.4 Current and capital spending

The Government has also set out the planned split between current and capital spending (see table below). Current spending will fall by 1% in real terms by 2015/16 while gross investment will fall by 31%. It is worth noting that large cuts in capital spending were included in the Labour Government's Budget in March. The June Budget said there would be no further cuts in capital spending beyond those already announced as part of the £6.2 billion of savings for 2010/11.[23] The Government has said that capital spending will be allocated to areas which "achieve the greatest economic returns."[24]

Current and capital spending *£ billion (2010/11 prices) (a)*

	Current	Gross investment (b)	Total
2010-11	637.3	59.5	696.8
2011-12	639.0	47.9	686.8
2012-13	637.4	44.6	682.1
2013-14	634.5	40.5	675.1
2014-15	630.6	40.9	671.4
2015-16	630.6	40.9	671.5
% change 2010/11 to 2015/16	-1%	-31%	-4%

Sources: HM Treasury, June 2010 Budget, Table 2.3 p45
Library calculations

Notes: (a) figures converted to 2010/11 prices using GDP deflator
(b) gross investment is the sum of net investment and depreciation

4.5 Protected and unprotected spending

The Government has made commitments to protect health and overseas aid spending. It has guaranteed that health spending will increase in real terms in each year of this Parliament

[23] HM Treasury, *Budget 2010*, June 2010, para 1.38

and that 0.7 per cent of gross national income with be spent on overseas aid by 2013.[25] As health is such a large budget, this commitment means that spending cuts for unprotected departments will be greater.

4.6 Additional welfare savings

The Chancellor said in the Budget that any further AME savings could be used to reduce the size of cuts to departmental budgets.[26] He reiterated this point in the House of Commons on 13 September 2010:

> The position on welfare is exactly as I set out in my Budget speech at this Dispatch Box when I said that if we could find further savings on welfare, we would be able to reduce the pressure on other Departments.[27]

On 4 October 2010, the Chancellor announced changes to the welfare system.[28] From 2013, there will be a cap on total household benefit payments. In addition, child benefit will be withdrawn from households which include a higher rate taxpayer by 2013. The Government estimates that the changes to child benefit will save £1 billion a year out of a total of £12 billion. The OBR will provide a more detailed estimate in the Spending Review.

5 What will be announced in the Spending Review?

As noted above, the Government has already announced the planned level of total public spending to 2015/16. The Spending Review will set out how this will be divided between DEL and AME and announce each department's DEL for the four years from 2011/12 to 2014/15 (inclusive). It will also set the DELs for the devolved administrations. The Spending Review will also announce plans for any further savings and reforms of social security, tax credits and public service pensions.[29]

The Spending Review will thus provide details of where the cuts will fall. As the overall level of public spending is forecast to fall and some areas of public spending, such as health, are protected, the cuts are expected to be severe for other departments. The Budget indicated that once commitments on health and overseas aid spending are taken into account, unprotected departments could see average real terms cuts of 25% over the four years covered by the review. If further AME savings are identified, this will reduce the size of cuts to departmental budgets.[30] The Budget figure of 25% is an average for unprotected departments so some could see even greater cuts. Press reports indicated that most departments had been asked to submit plans for cuts of up to 40% to the Treasury in July.[31] The Institute for Fiscal Studies have commented on the scale of the challenge as follows:

> Essentially, the plans laid out by the coalition government imply the longest and deepest sustained period of cuts to public service spending since at least the Second World War. It is clear that this will reduce the quantity or quality of public services available. Even the holy grail of efficiency savings cannot make this painless.

24 HM Treasury, *Budget 2010*, June 2010, para 2.16
25 HM Treasury, *The Spending Review framework*, June 2010, Cm 7872, para 1.8
26 HM Treasury, *Budget 2010*, para 1.40
27 HC Deb 13 September 2010 c601
28 HM Treasury Press Notice, *Chancellor announces reforms to welfare system*, 4 October 2010
29 HM Treasury, *Budget 2010*, June 2010, para 1.39
30 HM Treasury, *Budget 2010*, June 2010, para 1.40
31 "Whitehall winces as Osborne calls time", *Financial Times*, 17 July 2010

However, it is by no means obvious which public services will be maintained and which will be cut back or will simply have to fall by the wayside. This will not be revealed until the Spending Review this autumn, which will set out the budget each government department can expect in each year until the end of the Parliament in 2014/15.

[...]

Among the 'unprotected' departments, the axe will probably not be felt equally; some will do better than average and others worse. In his Budget speech, Chancellor George Osborne stated: 'I recognise, for example, the particular pressures on our education system and on defence' – implying perhaps that defence and parts of education spending might be less harshly cut come the Spending Review. Of course, this will come at an even greater cost to all other departments.

If the NHS received no real increase in spending and if spending on defence and schools were cut by 'only' 10% by 2014/15, this would leave the other departments facing cuts to their budgets of around a third. Such cuts would be extremely painful for the spending areas in question, which include transport, housing, higher education, public order and safety, and the central government grant to local authorities.

The government has also said that some areas of non-departmental spending will be considered for cuts in the Spending Review. Therefore, to some extent the severe squeeze on departments could be lessened by reducing other government spending. This would essentially amount to cutting social security spending and/or increasing employee contributions to public service pensions (which would cut the net payment by the Exchequer to members of these schemes each year).

However, even to reduce the average budget cuts facing unprotected departments from 25% to 20% would require £13bn of cuts, in today's prices, to be found from these other spending areas. Cuts of this size might not be easy to find: the combined effect of all the measures in the June Budget managed to shave around £10bn off welfare spending, and the remaining pot from which further savings would have to be found is only around £154bn.[32]

6 Impact of spending cuts

As the details of the Spending Review are not announced until 20 October, it is not possible to be certain about its impact. Nevertheless, it is possible to make some estimates of the possible impact based how public money is currently spent. The sections below summarise some studies which look at possible effects on employment, different areas of the UK and income groups.

6.1 Employment

The Office for Budget Responsibility forecasts that overall employment will increase by 1.3 million between 2010/11 and 2015/16. Public sector employment, however, is forecast to fall by 600,000.[33] While this forecast is affected by a wide range of economic factors, the planned level of public spending is likely to be an important factor.

The Government has announced that 192 quangos are to be axed but it is unclear how many jobs will be lost as a result.[34] A recent PwC report estimated that up to 500,000 private

[32] "*The axeman cometh*", Rowena Crawford and Gemma Tetlow (IFS), Public finance website, 10 July 2010
[33] Office for Budget Responsibility, *OBR forecast: Employment*, 30 June 2010
[34] Cabinet Office Press Release, *Quango reforms herald new age of accountability in Government*, 14 October 2010

sector jobs could be lost as a result of the spending cuts.[35] However the report went on to say:

> The fact that the public spending cuts will, considered in isolation, imply large job losses in both the public and private sectors should not therefore be taken to imply that the situation would be better had this fiscal squeeze not taken place: on the contrary, it is likely that the long run performance of the economy would have been even worse in that case due to higher interest rates and a greater risk of financial crisis.[36]

6.2 Regional impact

The BBC commissioned research from Experian which looked at the economic resilience of local authority areas in England. Experian point out that this research does not show which areas will suffer the most from spending cuts. Rather it "takes a holistic view of local areas and ranks them in terms of their ability to respond to economic shocks, such as public sector cuts".[37] The rankings are based on four themes: business, community, people and place. Business has the highest weighting. The research takes a wide range of social and economic factors into account, including industrial structure, skills, unemployment, crime rates and house prices.[38] According to this research, the least resilient areas are in the Midlands and North, while the most resilient are in London, the South and the East. The rankings and a map are available on the BBC website. The three most resilient areas were Elmbridge, St Albans and Waverley and the least resilient were Middlesbrough, Mansfield and Stoke-on-Trent.

The public sector accounts for a relatively large share of the economies of Northern Ireland, Scotland, Wales and the North of England measured by both employment and public spending (see table below). This suggests that these regions may be at greater risk from the spending cuts. The PwC report also found that Northern Ireland, Scotland, Wales and the North East are the areas most likely to suffer due to their reliance on public sector employment.[39]

The Government has said that it will limit as far as possible the impact of reductions in spending on the most vulnerable in society, and on those regions heavily dependent on the public sector. It has said that it aims to support the private sector in all parts of the UK. It has announced a Regional Growth Fund for England and a national insurance holiday to help new businesses setting up outside London, the South East and the East of England.

35 PwC, *Sectoral and regional impact of the fiscal squeeze*, October 2010
36 PwC, *Sectoral and regional impact of the fiscal squeeze*, October 2010, p3
37 Index of Resilience – Experian Methodology
38 Details of the methodology are available on the BBC website.
39 PwC, *Sectoral and regional impact of the fiscal squeeze*, October 2010, p2

Public spending and public sector employment by region

Region	Public sector employment as % of total employment Q2, 2010	Region	Public spending per head UK = 100 2009/10
Northern Ireland	29.4%	Northern Ireland	121
Wales	26.1%	London	115
Scotland	24.8%	Scotland	115
North East	24.7%	North East	109
Yorks & Humber	22.1%	Wales	109
North West	21.9%	North West	105
London	20.9%	West Midlands	98
West Midlands	20.6%	Yorks & Humber	95
South West	20.6%	South West	92
East Midlands	18.3%	East Midlands	90
South East	16.5%	South East	87
East	16.5%	East	86
UK	20.9%	UK	100

Sources: HM Treasury and Library calculations based on ONS data

The Library has also published information on "public sector" employment by Parliamentary constituency. While a number of caveats need to be borne in mind when interpreting these data[40], they show that of the ten constituencies with the highest rates of "public sector" employment in 2008, seven are in Scotland, the North West or North East.

6.3 Impact by income group

Andrew Tyrie MP, chairman of the Treasury Committee, asked the Chancellor whether the spending review would include a full analysis of all the measures broken down by decile (ie each 10% of the income distribution). The Chancellor replied that he would try to provide the best available information but that analysing the effect of all the expenditure changes was difficult.[41]

Research carried out for the TUC argued that the poorest would be affected most by the spending cuts. A TUC press release said:

> The UK's poorest 10 per cent will be hit 13 times harder by spending cuts than the richest ten per cent according to new research, drawn from the most comprehensive analysis of the effects of UK public spending ever undertaken, and published on the eve of the TUC Congress in Manchester today (Sunday).
>
> The research - Where The Money Goes - shows that the bottom 10 per cent of the population will suffer reductions in services equivalent to 20 per cent of their household income, while the richest 10 per cent will lose the equivalent of just 1.5 per cent from

[40] There are no official data published for public sector employment by constituency. A proxy for the public sector is used. The data are based on where a person works rather than where they live and are subject to sampling error. For further details, please see *Public sector employment by Parliamentary constituency*, SN/EP/5635

[41] HC Deb 13 September 2010 c604-5

cuts that the Government plans to implement by 2013. Across the income distribution, the poorer the household, the more they will lose.

[...]

The study shows that lone parents (11 per cent) and single pensioners (9 per cent) are the social groups that lose the most, while childless couples stand to lose the least (3 per cent).

The study examines the impact of the cuts on four typical families:

A typical family with two young people on modest earnings will suffer cuts equivalent to 6.2 per cent of their income.

An affluent family with student children will suffer cuts equivalent to 4.2 per cent of their income.

A working lone parent with two children will suffer cuts equivalent to 10.4 per cent of her income.

A pensioner couple will suffer cuts equivalent to 16.2 per cent of their income

The study also shows that cuts will reinforce the North/South divide in England. Households in the North East will lose services equivalent to six per cent of their household income, while Londoners will lose less than four per cent.[42]

Researchers at the IFS argue, however, that attempting to judge the progressivity or otherwise of cuts in public spending is difficult and attempts to do so should be treated with caution:

> Given the difficulties, conceptual and empirical, involved in the valuation of the benefits of public services, producing a single set of numbers that represent the distributional impact of the entire package of cuts to spending on public services necessarily involves making a series of contentious assumptions which may crucially impact the outcome; an alternative and no less plausible set of assumptions could yield quite a different outcome. For this reason, we suggest such exercises are interpreted with caution. The best approach is perhaps to put bounds on what constitutes a reasonable opinion about what the distributional effects may be rather than trying to tie things down to a single answer.[43]

The *Guardian's* website includes information on how the reductions in public spending are affecting various public services.

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[42] TUC Press Release, *Spending cuts will hit the poorest 13 times harder than the richest,* 13 September 2010. The full report is *Where the money goes: How we benefit from public services*, by Tim Horton and Howard Reed, 12 September 2010

[43] *Can we assess the distributional impact of cuts to spending on public services,* Cormac O'Dea and Ian Preston, IFS Observations, October 2010

7 Public spending data

Total public spending

	£ billion current prices	£ billion real terms (a)	Annual growth real terms %	% GDP
1970-71	22.7	267.6	3.3%	42.7%
1971-72	25.2	272.8	1.9%	42.6%
1972-73	28.2	281.3	3.1%	41.9%
1973-74	33.4	310.7	10.5%	44.3%
1974-75	43.7	339.8	9.4%	48.6%
1975-76	55.7	345.4	1.6%	49.7%
1976-77	63.6	347.2	0.5%	48.5%
1977-78	69.4	333.2	-4.0%	45.6%
1978-79	78.5	339.6	1.9%	45.1%
1979-80	93.5	346.0	1.9%	44.6%
1980-81	112.4	351.8	1.7%	47.0%
1981-82	125.5	358.8	2.0%	47.8%
1982-83	138.3	370.0	3.1%	48.1%
1983-84	149.7	382.9	3.5%	47.8%
1984-85	159.9	388.4	1.4%	47.5%
1985-86	166.5	382.9	-1.4%	45.0%
1986-87	172.7	384.8	0.5%	43.6%
1987-88	183.3	386.3	0.4%	41.6%
1988-89	190.7	376.4	-2.6%	38.9%
1989-90	210.2	387.3	2.9%	39.2%
1990-91	227.5	388.5	0.3%	39.4%
1991-92	254.2	409.8	5.5%	41.9%
1992-93	274.2	428.9	4.6%	43.7%
1993-94	286.0	435.4	1.5%	43.0%
1994-95	299.0	448.2	2.9%	42.5%
1995-96	311.0	453.2	1.1%	41.8%
1996-97	315.9	443.8	-2.1%	39.9%
1997-98	322.0	440.8	-0.7%	38.2%
1998-99	330.9	443.6	0.6%	37.2%
1999-00	343.0	451.0	1.7%	36.3%
2000-01	364.0	472.4	4.7%	36.8%
2001-02	389.2	494.0	4.6%	37.7%
2002-03	421.2	518.0	4.8%	38.6%
2003-04	455.5	544.8	5.2%	39.4%
2004-05	492.4	573.0	5.2%	40.5%
2005-06	524.0	598.9	4.5%	41.1%
2006-07	550.0	608.2	1.6%	40.8%
2007-08	582.5	626.2	3.0%	40.9%
2008-09	629.6	658.7	5.2%	43.9%
2009-10	669.8	689.2	4.6%	47.7%
2010-11	696.8	696.8	1.1%	47.3%
2011-12	699.8	686.8	-1.4%	45.5%
2012-13	711.0	682.1	-0.7%	43.9%
2013-14	722.0	675.1	-1.0%	42.2%
2014-15	737.5	671.4	-0.5%	40.9%
2015-16	757.5	671.5	0.0%	39.8%

Sources: HM Treasury, Public finances databank, Tables B1 and B2, Library calculations

Notes: (a) 2010/11 prices calculated using GDP deflator

8 Links to further information

HM Treasury http://www.hm-treasury.gov.uk/home.htm

June Budget: http://www.hm-treasury.gov.uk/junebudget_documents.htm

Spending Review: http://www.hm-treasury.gov.uk/spend_index.htm

Spending challenge: http://spendingchallenge.hm-treasury.gov.uk/

The Spending Review Framework, June 2010, Cm 7872 http://www.hm-treasury.gov.uk/d/spending_review_framework_080610.pdf

Public Expenditure Statistical Analyses (PESA), July 2010, Cm 7890, http://www.hm-treasury.gov.uk/pespub_pesa10.htm

March Budget: http://webarchive.nationalarchives.gov.uk/20100407010852/http://www.hm-treasury.gov.uk/budget2010.htm

2007 Spending Review:
http://webarchive.nationalarchives.gov.uk/20100407010852/http://www.hm-treasury.gov.uk/pbr_csr07_index.htm

Office for Budget Responsibility http://budgetresponsibility.independent.gov.uk/

Sir Philip Green Report:
http://download.cabinetoffice.gov.uk/efficiency/sirphilipgreenreview.pdf

Institute for Fiscal Studies http://www.ifs.org.uk/

"The axeman cometh" Rowena Crawford and Gemma Tetlow, Public Finance website 10 July 2010: http://www.publicfinance.co.uk/features/2010/07/the-axeman-cometh/

Post-Budget Briefing (June 2010): http://www.ifs.org.uk/projects/330

House of Commons Library

Monthly *Economic Indicators* Research Paper:
http://hcl1.hclibrary.parliament.uk/wdw/subject/ei.asp (Parliamentary users).

Other users may access this from:
http://www.parliament.uk/business/publications/research/research-papers/research-papers-2010/

Other reports on the Spending Review

BBC Spending Review website:
http://www.bbc.co.uk/news/special_reports/spending_review/

TUC, *Where the money goes: How we benefit from public services*, by Tim Horton and Howard Reed, 12 September 2010, http://www.tuc.org.uk/extras/wherethemoneygoes.pdf

PwC, *Sectoral and regional impact of the fiscal squeeze*, October 2010, http://psrc.pwc.com/pdf/impact_of_fiscal_squeeze.pdf