

## 7. Pressures on public spending

Alastair Muriel and Luke Sibieta (IFS)

### Summary

- Public spending is set to grow only half as quickly over the three years covered by the 2007 Comprehensive Spending Review (CSR) as over the ‘years of plenty’ covered by the previous four spending reviews. In a number of areas, the CSR spending plans may be insufficient to achieve stated policy goals.
- Health is set to see spending increase much less quickly than it has done over recent years. The CSR proposes to spend between £6 billion and £10 billion less on health in 2010–11 than Sir Derek Wanless’s reviews have suggested would be necessary to progress towards a world-class health service.
- Education spending will stop rising as a share of national income under the CSR plans. If spending continues to increase at the rate planned in the CSR, the government would only meet its goal of matching the 2005–06 level of spending per pupil in the private sector in 2020–21 – a lag of 15 years.
- The local government settlement between 2008 and 2010, and the prospect of ‘capping’ for councils that propose cash-terms increases in council tax rates above 5%, put pressures on local services. These could be particularly tight in 2010–11, when the main grant is set to be cut in real terms.
- The government would need to spend around £3.4 billion more than it is currently forecasting on tax credits and social security benefits in 2010–11 if it were to give itself a 50:50 chance of meeting its child poverty target for that year.

### 7.1 Introduction

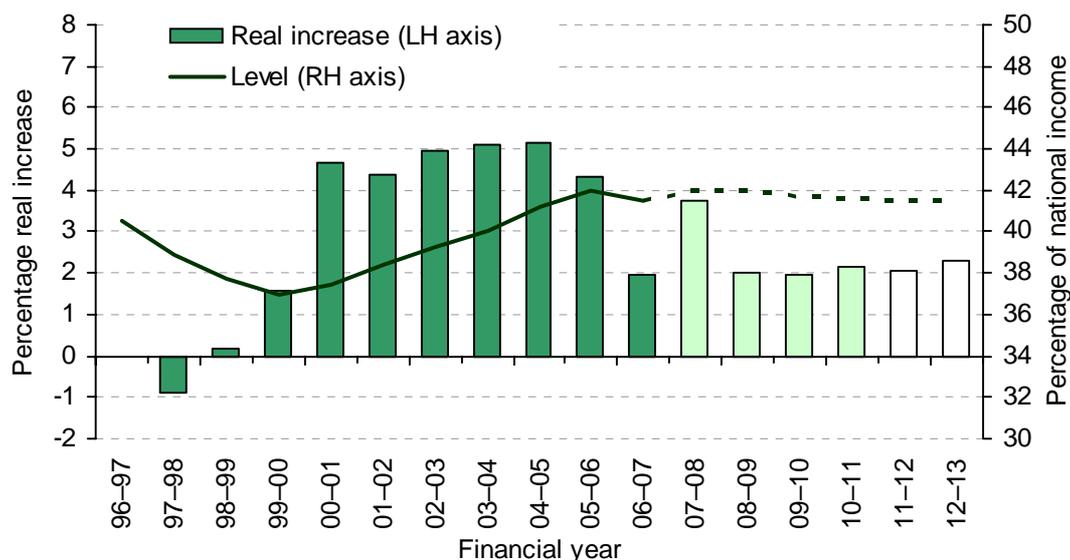
The 2007 Comprehensive Spending Review (CSR) set out plans for the level and composition of public spending in 2008–09, 2009–10 and 2010–11. On average, spending is set to increase by only 2.1% per year in real terms over this period, only half the rate seen during the ‘years of plenty’ covered by the previous four spending reviews. By reducing the growth rate of public spending below that expected for the economy, these plans would cut public spending from 42.0% of national income in 2007–08 to 41.6% by 2010–11. Given this planned squeeze, will there be sufficient resources to deliver on the government’s key policy goals?

Section 7.2 summarises the trends in aggregate public spending under Labour. In Section 7.3, we discuss whether or not the real increases in spending allocated in the 2007 CSR are likely to be sufficient to achieve the government’s main objectives in seven important policy areas: health, education, child poverty, local government, defence, transport and international aid. (The important issue of the setting of public sector pay, which represents one-third of total government expenditure, is discussed in Chapter 8.) Section 7.4 concludes.

## 7.2 Trends in aggregate public spending under Labour

This section discusses the trends in aggregate public spending under Labour. The bars in Figure 7.1 show the percentage annual real increases (left-hand axis) in total public spending (technically known as total managed expenditure or TME) under Labour to date and the line shows total public spending as a proportion of national income (right-hand axis).

Figure 7.1. Total public spending



Sources: Total managed expenditure from table B1 of HM Treasury, *Public Sector Finances Databank*, December 2007 ([http://www.hm-treasury.gov.uk/media/B/2/pfd\\_211207.xls](http://www.hm-treasury.gov.uk/media/B/2/pfd_211207.xls)) and table B5 of HM Treasury, *2007 Pre-Budget Report and Comprehensive Spending Review*, October 2007 ([http://www.hm-treasury.gov.uk/pbr\\_csr/report/pbr\\_csr07\\_repindex.cfm](http://www.hm-treasury.gov.uk/pbr_csr/report/pbr_csr07_repindex.cfm)). GDP and GDP deflators up-to-date as of 20 December 2007 from HM Treasury website ([http://www.hm-treasury.gov.uk/media/6/8/GDP\\_Deflators\\_20071220\\_NA\\_update\\_circ.xls](http://www.hm-treasury.gov.uk/media/6/8/GDP_Deflators_20071220_NA_update_circ.xls)).

Labour came into office in 1997 having promised to abide by the tight public spending plans that it inherited from the Conservatives for two financial years. It largely kept this promise, cutting spending by 0.4% a year in real terms on average. It was helped by robust economic growth (which kept social security bills down) and by falling debt interest costs.

In July 1998, the government published its first CSR, which set out plans for 1999–2000, 2000–01 and 2001–02. With tax revenues buoyant and the public finances strengthening, the Treasury sanctioned an increase in total spending of 3.3% a year in real terms. But largely because departments failed to spend the money they had been allocated in the first year of the review, spending rose by only 1.6% in 1999–2000 – less than the growth rate of the economy. As a result, spending had fallen by more than 3% of national income over Labour’s first three years in office, from 40.6% in 1996–97 to 37.0% in 1999–2000.

Thereafter, Labour increased spending rapidly, pumping money into public services (especially education and health, as described in Section 7.3) and transfer payments (notably benefit and tax credit payments for lower-income families with children and lower-income pensioners – see Chapter 14). Spending grew by more than 4% a year for six successive years, taking it to 42.0% of national income in 2005–06.

In the July 2004 Spending Review (SR), the government began gently to apply the brakes. The Treasury's original plans showed real increases declining from 4.2% in 2005–06 to 2.6% in 2006–07 and 2.8% in 2007–08. In fact, spending growth came in at a higher-than-intended 4.3% in 2005–06 and then slowed more sharply than intended to 2.0% in 2006–07. The Treasury now expects spending growth to rebound to 3.8% this year, giving an average increase of 3.3% a year over the three years of the review – slightly more than the 3.2% set down in the original plans. The unexpectedly weak figure for spending growth in 2006–07 reflects the fact that cash-terms public spending came in at £550.0 billion, £4.6 billion lower than the government's planned level of £554.6 billion (as set out in Spending Review 2004). The difference can mostly be accounted for by a £2.9 billion underspend in health and a £1.0 billion underspend in education, both compared with their respective planned levels for 2006–07 as set out in Spending Review 2004.

Public spending plans for 2008–09, 2009–10 and 2010–11 were set out in last year's CSR. Public spending is projected to grow by 2.0% in real terms in both 2008–09 and 2009–10, and then by 2.1% in 2010–11. As shown by the dotted line in Figure 7.1, this would mean public spending declining to 41.6% of national income in 2010–11. This 0.4% of national income cut in public spending is equivalent to £6 billion in 2007–08 terms.

The projected level of spending in 2010–11 would be higher than that inherited by Labour when it came to power (40.6% of national income), but lower than the average seen during either John Major's premiership (42.9% of national income) or Margaret Thatcher's (44.9% of national income).

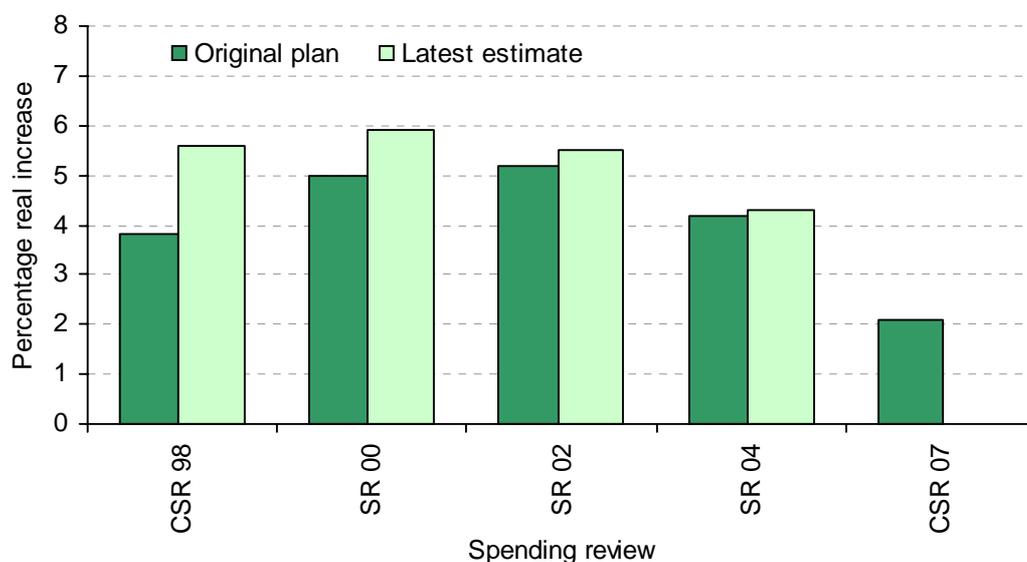
Last year's Pre-Budget Report (PBR) also presented projections for cash spending in 2011–12 and 2012–13. Figure 7.1 shows what these projections, if adopted as firm plans and then delivered in full, would mean in terms of annual real increases and for public spending as a proportion of national income (assuming inflation of 2.7% per year and projected levels of national income as published in the PBR). These increases, if delivered in full, would amount to slightly larger annual real increases than the planned real increases for the period from 2007–08 to 2010–11, at 2.1% for 2011–12 and 2.3% for 2012–13. These plans, if delivered in full, would also lead public spending as a proportion of national income to decline by a further 0.2% to reach 41.5% in 2012–13.

Actual real increases in public spending have differed from original spending plans over spending reviews under Labour to date. Part of this is due to the fact that actual inflation has differed from expected inflation, but it is also due to the fact that the government may decide to allocate more resources to departments and top up their spending plans. Figure 7.2 shows the annualised average real increase in departmental spending as set out in CSR 98, SR 2000, SR 2002, SR 2004 and CSR 2007. These are adjusted for subsequent inflation, which means they show the after-inflation increase that would have occurred had the original cash spending plans been delivered. The graph also shows actual real increases in departmental spending across these same periods. It is quite clear from this comparison that the original 'firm and fixed' cash spending plans over the periods covered by CSR 98, SR 2000 and SR 2002 were subsequently topped up. However, the tendency to top up spending plans appears to be declining over time – presumably reflecting the fact that the weakening outlook for the public finances left less money for the government to play with. Spending plans over the period

covered by SR 2004 were topped up slightly, but by a much smaller margin than for CSR 1998 and SR 2000.

Public spending has not grown steadily under Labour. In fact, it has seesawed from average real-terms cuts in their first two years of office, real increases above 4% between 2000–01 and 2005–06 and has now swung back to a planned real increase of 2.1% between 2007–08 and 2010–11. It also clear that spending plans are not necessarily firm and fixed. They have instead been topped up in subsequent years, though the tendency for the government to do this has reduced over time. The next section looks at pressures that might prompt government to diverge from its plans for the period covered by last year’s CSR.

Figure 7.2. Firm and fixed departmental spending plans?



Note: Departmental spending refers to the total of all departmental expenditure limits.  
 Sources: Departmental expenditure limits and GDP deflators as for Figure 7.1; initial cash spending plans (adjusted for subsequent inflation) taken from table 3 of C. Emmerson and G. Tetlow, *The 2007 Comprehensive Spending Review: A Challenging Spending Review?*, IFS Briefing Note 75, 2007 (<http://www.ifs.org.uk/bns/bn75.pdf>).

### 7.3 Trends in key areas of public spending

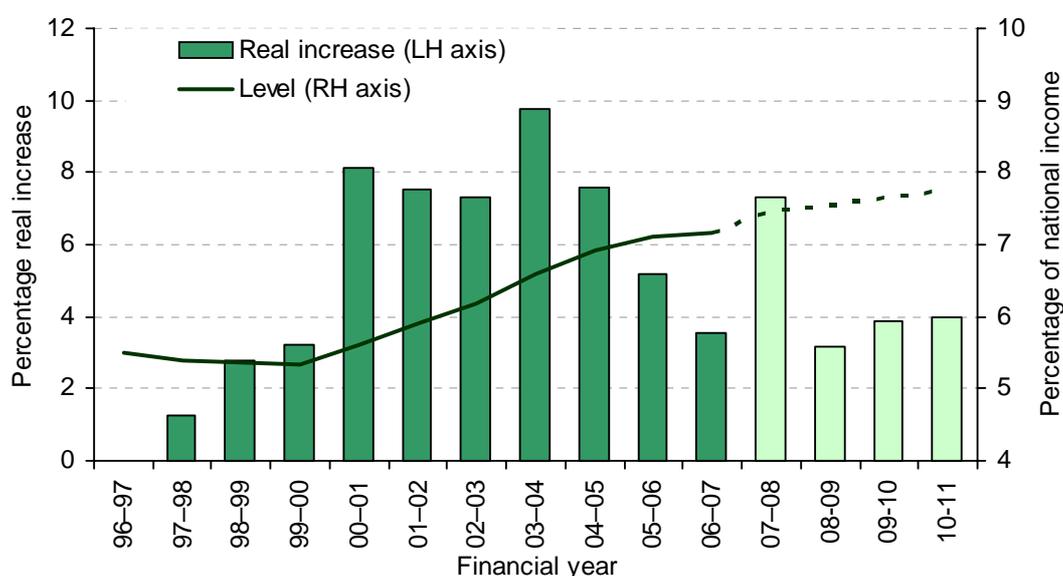
While the government’s plans show public spending as a whole increasing in real terms by 2.1% a year over the period of the 2007 CSR, different departments and areas of spending have received different allocations – from a 5.6% real cut each year for the administrative part of the Department for Work and Pensions to a 3.7% real increase per year in health. To what extent are these allocations consistent with the government’s stated policy goals in each area? Might the government need to top up these plans or scale back its ambitions?

In this section, we look at the spending plans in seven areas: health, education, child poverty, local government, defence, transport and international aid.

## Health

The past seven years have seen the largest sustained increase in funding for the National Health Service since its inception in 1949.<sup>1</sup> The Treasury-commissioned Wanless Review of healthcare expenditure, published alongside the April 2002 Budget, recommended that to close the ‘considerable gaps in performance between the UK and other developed countries’, NHS spending would need to grow more quickly than the economy at least until 2017–18.<sup>2</sup> Although the government never formally promised to follow Wanless’s recommendations, Gordon Brown cited this conclusion in his 2002 Budget, announcing a five-year settlement for the NHS that promised average real-terms increases of 7.4% per year for the five years from 2003–04 to 2007–08.

Figure 7.3. Health spending



Note: Figures refer to public sector health spending based on the UN Classification of the Functions of Government (COFOG), the international standard, as used in the Public Expenditure Statistical Analysis.

Sources: Period to 2006–07 from HM Treasury, *Latest Functional Data*, October 2007 ([http://www.hm-treasury.gov.uk/media/6/1/PBR\\_2007\\_functional\\_series.xls](http://www.hm-treasury.gov.uk/media/6/1/PBR_2007_functional_series.xls)). Period from 2007–08 onwards from table D6 of HM Treasury, *2007 Pre-Budget Report & Comprehensive Spending Review*, October 2007 ([http://www.hm-treasury.gov.uk/media/4/7/pbr\\_csr07\\_annexd2\\_197.pdf](http://www.hm-treasury.gov.uk/media/4/7/pbr_csr07_annexd2_197.pdf)). This assumes real growth in national income of 2½% per year, the Treasury’s ‘cautious’ assumption for real GDP growth used for its public finance projections.

Figure 7.3 shows UK health spending as a percentage of national income up until 2006–07, together with plans for 2007–08 to 2010–11, assuming they are delivered in full. Also shown in the graph is the real increase in health spending each year implied by these actual and planned levels of health spending. The real increases in health spending during Labour’s first three years in office were lower than growth in the economy – therefore health spending declined slightly as a share of national income (from 5.5% of national income in 1996–97 to 5.3% of national income in 1999–2000). However, from 2000–01 onwards (even before the Wanless Review was published), the government introduced significant spending increases of

<sup>1</sup> For more details of NHS spending over time, see C. Emmerson, C. Frayne and A. Goodman, *Pressures in UK Healthcare: Challenges for the NHS*, IFS Commentary 81, May 2000 (<http://www.ifs.org.uk/comms/nhsspending.pdf>).

<sup>2</sup> D. Wanless, *Securing Our Future Health: Taking a Long-Term View*, April 2002 ([http://www.hm-treasury.gov.uk/Consultations\\_and\\_Legislation/wanless/consult\\_wanless\\_final.cfm](http://www.hm-treasury.gov.uk/Consultations_and_Legislation/wanless/consult_wanless_final.cfm)).

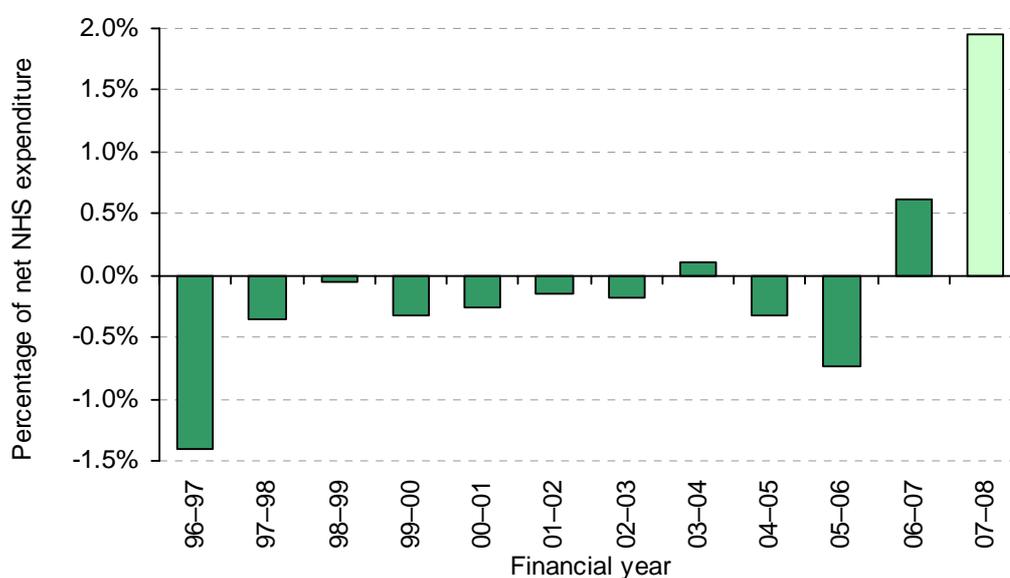
more than 7% per year in real terms. If plans set out in the 2007 CSR are delivered in full, public spending on healthcare is projected to reach 7.8% of national income in 2010–11, which would be its highest ever level.

However, Figure 7.3 also makes clear how volatile these spending increases have been. While the 2002 Budget promised steady annual spending increases of between 7.2% and 7.7% per year, in reality growth has been far less consistent. Spending growth was as high as 9.8% in 2003–04, before falling to 3.5% in 2006–07.

The cycle of first overshooting then undershooting expenditure plans has seen the NHS budget move from a deficit of over £500 million in 2005–06 to a predicted surplus of up to £1.8 billion in 2007–08.<sup>3</sup> While the deficits of 2004–05 and 2005–06 generated considerable media coverage, they were by no means unprecedented, as Figure 7.4 shows. England’s NHS deficit in the last year of John Major’s administration, at 1.4% of net NHS expenditure, was twice the size of the deficit in 2005–06 (0.7% of net NHS expenditure). Indeed, the health service had run small deficits for seven of the eight years prior to 2005–06. At least compared with recent history, it is the comparatively large surpluses generated in 2006–07 and 2007–08 (under current plans) that are anomalous.

The net result of this over- and under-spending is that health spending has on average grown more slowly than Mr Brown had planned in 2002, with average real growth of 6.6% per year between 2002–03 and 2007–08 rather than the 7.4% annual growth announced in 2002.

Figure 7.4. NHS budget deficit/surplus in England



Sources: Authors’ calculations based on time series of NHS deficits from House of Commons Health Committee, *NHS Deficits*, December 2006 (<http://www.publications.parliament.uk/pa/cm200607/cmselect/cmhealth/73/73i.pdf>) and series on net NHS expenditure created from Department of Health Annual Reports, 2001 to 2007 (<http://www.dh.gov.uk/en/Publicationsandstatistics/Publications/AnnualReports/index.htm>).

<sup>3</sup> Sources: Department of Health, *NHS Financial Performance, Quarter 4 2006–07*, June 2007 ([http://www.dh.gov.uk/en/Publicationsandstatistics/Publications/PublicationsPolicyAndGuidance/DH\\_075230](http://www.dh.gov.uk/en/Publicationsandstatistics/Publications/PublicationsPolicyAndGuidance/DH_075230)); Department of Health, *The Quarter: Quarter 2, 2007–08* (NHS Financial Performance), November 2007 ([http://www.dh.gov.uk/en/Publicationsandstatistics/Publications/PublicationsPolicyAndGuidance/DH\\_080967](http://www.dh.gov.uk/en/Publicationsandstatistics/Publications/PublicationsPolicyAndGuidance/DH_080967)).

Looking ahead, the government currently plans to increase healthcare spending by 3.7% a year on average in real terms between 2008–09 and 2010–11. How do these growth rates compare with those recommended in the Wanless Review? The review set out three different scenarios for NHS spending based on different assumptions regarding the efficiency of the NHS and the contribution that the population makes to its own health through its own behaviour:

- ‘Slow uptake’ – the most expensive scenario. This assumes that the health status of the population is constant or deteriorates, with the public failing to become more ‘engaged’ with improving its own health. Life expectancy still increases, but by the smallest amount of all scenarios. The health service is assumed to be relatively unresponsive, with low rates of technology uptake and low productivity. Under this scenario, spending would need to grow by 7.4% a year between 2002–03 and 2007–08 and then by 5.6% a year between 2007–08 and 2012–13.
- ‘Solid progress’: This requires increasing public engagement with health, improving health status and increasing life expectancy. The health service becomes more responsive, with high rates of technology take-up and more efficient use of resources. Under this scenario, spending would need to grow by 7.1% a year between 2002–03 and 2007–08 and then by 4.7% a year between 2007–08 and 2012–13.
- ‘Fully engaged’ – the least expensive scenario. This requires high engagement by the public with its health, dramatically improving health status and with life expectancy increasing beyond current forecasts. It also requires high rates of technology and more efficient use of resources by the NHS. Under this scenario, spending would need to grow by 7.1% a year between 2002–03 and 2007–08 and then by 4.4% a year between 2007–08 and 2012–13.

In a report commissioned by the King’s Fund five years after his original report, Sir Derek Wanless and co-authors estimated that in terms of services delivered, the NHS lay somewhere between the ‘slow uptake’ and ‘solid progress’ scenarios.<sup>4</sup> Public engagement was also judged to be on a path between ‘slow uptake’ and ‘solid progress’, though over-optimistic targets (on obesity, for example) mean that in some areas not even the ‘slow uptake’ scenario is being achieved. The NHS has also failed to realise the productivity gains assumed in the 2002 report, the authors suggest, placing the productivity of the health service closer to the ‘slow uptake’ scenario.

The real spending increase of 7.4% a year planned in Spending Review 2004 would have been sufficient under the ‘fully engaged’ scenario, but the increases of 6.6% that were actually delivered fell slightly short of that – and even further short of the increases required under the ‘slow uptake’ scenario. The 3.7% a year real increase proposed for the next three years under the CSR also falls short of what Wanless recommended under each scenario.

Where does this leave us with regard to the level of spending implicitly recommended by the 2002 Wanless Review? Table 7.1 shows the shortfall between planned government health expenditure in 2010–11 and Wanless’s recommended level of spending under each of the

---

<sup>4</sup> D. Wanless, J. Appleby, A. Harrison and D. Patel, *Our Future Health Secured?*, Kings Fund, September 2007 ([http://www.kingsfund.org.uk/publications/kings\\_fund\\_publications/our\\_future.html](http://www.kingsfund.org.uk/publications/kings_fund_publications/our_future.html)).

three scenarios, if plans going forward are delivered in full. Given the findings of the most recent Wanless Review (that the NHS is somewhere between the ‘slow uptake’ and ‘solid progress’ scenarios), the current spending gap is between £2.4 billion and £3.6 billion, and is set to widen to between £6.2 billion and £10.4 billion at the end of the CSR period in 2010–11 under current plans. This means that by 2010–11, health expenditure would be 5.1% below Wanless’s recommended spending under the ‘solid progress’ scenario and 8.2% below the spending level envisaged under ‘slow uptake’. To close the gap would require the government to spend between 1% and 1.2% of national income more on health in 2010–11 than it is currently planning to do.

**Table 7.1. NHS spending shortfall compared with Wanless recommendations**

	<b>Real spending shortfall in 2007–08</b>	<b>Real spending shortfall by 2010–11</b>	<b>Shortfall as % of Wanless recommended spending in 2010–11</b>
Slow uptake	£3.6 billion	£10.4 billion	8.2%
Solid progress	£2.4 billion	£6.2 billion	5.1%
Fully engaged	£2.4 billion	£5.0 billion	4.4%

Notes: Figures in £ billion at 2007–08 prices. Recommended spending levels have been calculated by starting with actual health spending in 2002–03 and applying the Wanless Report’s recommended annual growth rates under each scenario every year to 2010–11.

Sources: As for Figure 7.3; authors’ calculations.

## Education

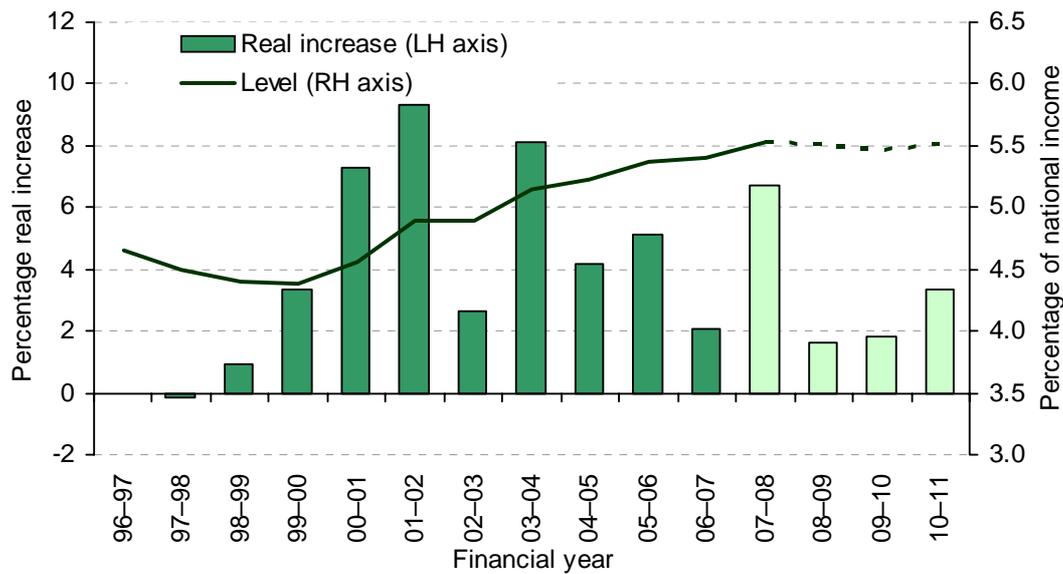
The current government has made a number of pledges with regard to education, some quantifiable, some less so. This section examines whether the recent CSR settlement is sufficient to meet the manifesto commitment to increase education spending as a share of national income. It also discusses the aspiration to increase state school spending to the level spent by the independent sector in 2005–06, plus the implications for education spending of the ambition for a ‘world-class education system’.

Figure 7.5 shows UK education spending as a proportion of national income up until 2006–07, together with the projected shares for 2007–08 and beyond, assuming the CSR settlement for education is delivered in full. Also shown in Figure 7.5 is the annual real increase in education spending for each year between 1996–97 and 2010–11 (figures for 2007–08 and beyond represent planned real increases).

Over Labour’s two complete terms of office, it is clear that education spending at the end of each Parliament was higher as a share of national income than it was at the start. The CSR settlement for education spending also means that this pledge is likely to be met over Labour’s third term, as education spending as a proportion of national income is projected to be higher in 2009 and 2010 (likely dates for the next general election) under current plans than it was in 2005.

However, it is important to note that the main reason these manifesto commitments have been met – or are likely to be met – is the very strong year-on-year increases between 1999–2000 and 2007–08. This means that the manifesto commitment was met by a very large margin indeed during Labour’s second term, as compared with much smaller margins over Labour’s

Figure 7.5. Education spending



Note: Education spending refers to public sector education spending based on the UN Classification of the Functions of Government (COFOG), the international standard, as used in the Public Expenditure Statistical Analysis.

Sources: Period to 2006–07 from HM Treasury, *Latest Functional Data*, October 2007 ([http://www.hm-treasury.gov.uk/media/6/1/PBR\\_2007\\_functional\\_series.xls](http://www.hm-treasury.gov.uk/media/6/1/PBR_2007_functional_series.xls)). Period from 2007–08 onwards from table D1 of HM Treasury, *2007 Pre-Budget Report & Comprehensive Spending Review*, October 2007 ([http://www.hm-treasury.gov.uk/media/3/9/pbr\\_csr07\\_annexd1\\_189.pdf](http://www.hm-treasury.gov.uk/media/3/9/pbr_csr07_annexd1_189.pdf)). This assumes real growth in national income of 2½% per year, the Treasury's 'cautious' assumption for real GDP growth used for its public finance projections.

first and potentially also during its third term. Over the period covered by the 2007 CSR, education spending as a share of national income is currently expected to remain at 5.5% of national income. This is despite the fact that Mr Brown has said that the coming years are a time when public and private spending on education, innovation and science should be increasing further as a share of national income:<sup>5</sup>

I believe that taking private and public investments together, advanced industrial countries will have in future [to] aspire to invest not 5-6-7-8 per cent of their national income, on education, science and innovation but 10 per cent, one pound in every ten.

As well as its manifesto commitment to increase education spending as a share of national income, the government has made other pledges with regard to increased levels of education spending. In Budget 2006, the then Chancellor, Gordon Brown, stated that:<sup>6</sup>

To improve pupil teacher ratios and the quality of our education, we should agree an objective for our country that stage by stage, adjusting for inflation, we raise average investment per pupil to today's private school level.

Meeting this aspiration would require increasing spending per pupil in the state sector (£5,280 in 2005–06 in today's prices) to reach the level seen in the independent sector in 2005–06 (£8,440 in today's prices). The CSR announced that state spending per pupil would reach the

<sup>5</sup> Speech by the Chancellor of the Exchequer, the Rt Hon. Gordon Brown, to Mansion House, 20 June 2007 ([http://www.hm-treasury.gov.uk/newsroom\\_and\\_speeches/press/2007/press\\_68\\_07.cfm](http://www.hm-treasury.gov.uk/newsroom_and_speeches/press/2007/press_68_07.cfm)).

<sup>6</sup> [http://www.hm-treasury.gov.uk/budget/budget\\_06/bud\\_bud06\\_speech.cfm](http://www.hm-treasury.gov.uk/budget/budget_06/bud_bud06_speech.cfm).

equivalent of £6,160 in 2007–08 prices under current plans. This leaves a remaining real-terms gap of £2,280 per pupil in 2010–11 (2007–08 prices) or a total of £17.2 billion.

The figures announced in the CSR imply that state school spending per pupil will grow by 3.2% per year in real terms between 2007–08 and 2010–11, if plans going forward are delivered in full. If this growth were continued beyond 2010–11, the aspiration would not be met until about 2020–21 – some 15 years after the same level of spending had been achieved in the private sector. Alternatively, if school spending per head were to grow at the underlying rate of growth in the economy (assumed to be the Treasury’s ‘cautious’ assumption of 2½% real per year) and thus remain constant as a share of national income, it would take until 2023–24 to meet the pledge – a lag of 18 years.

The implicit assumption made by politicians of all stripes when calling for higher education spending is that it would deliver improved educational attainment. Therefore it is worth asking whether countries with higher spending per pupil achieve better educational outcomes, and thus whether higher education spending will deliver a ‘world-class education system’, a stated ambition in a recent speech by the Prime Minister: ‘Our ambition must be nothing less than to be world class in education and to move to the top of the global education league’.<sup>7</sup>

The OECD recently published cross-country rankings in terms of students’ performance in reading, maths and science. This placed the UK 17<sup>th</sup> out of 56 OECD and partner countries in terms of reading, 24<sup>th</sup> out of 57 countries in terms of maths and 14<sup>th</sup> out of 57 countries in terms of science. Is spending per pupil higher in the countries ranked above the UK in these league tables, i.e. is spending per pupil higher in countries that have ‘world-class’ results? We will focus on performance in maths, since this was the UK’s lowest ranking out of these three core subjects and thus where the UK appears to have furthest to go in order to become ‘world-class’.

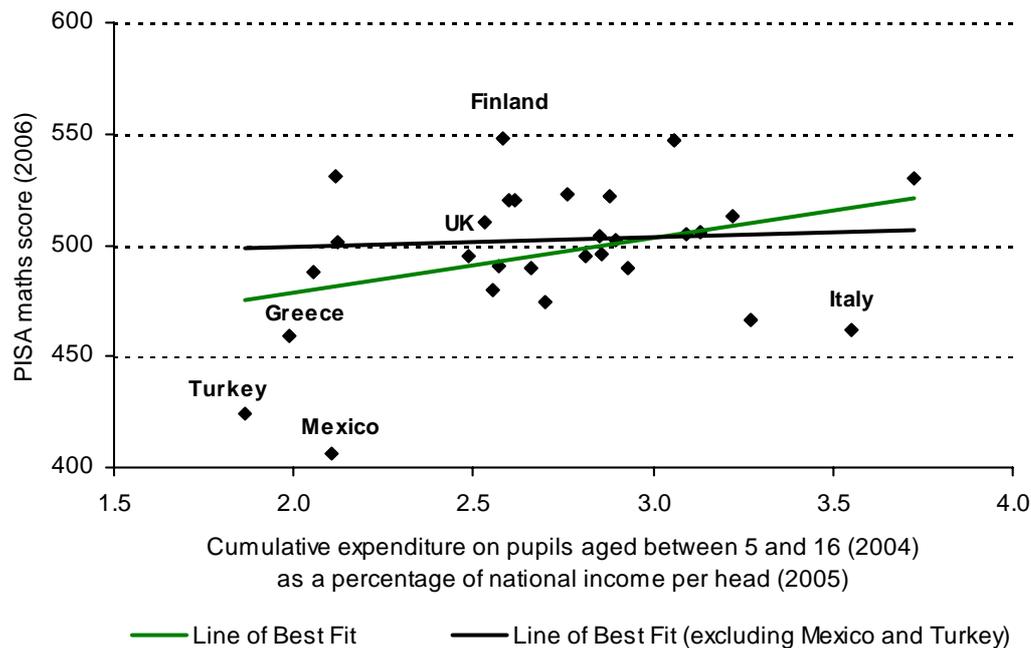
Figure 7.6 shows students’ average performance in maths against a measure of education spending per pupil scaled by national income per head for OECD countries (this excludes partner countries present in the league tables). Education spending per pupil is measured as the cumulative expenditure per student throughout primary and secondary schooling in 2004 (between the ages of 5 and 16). We then divide this by each country’s respective national income per head in 2005. Average performance is measured by students’ average score in PISA maths assessments in 2006. (Note that graphs showing PISA reading and science results instead of maths give a very similar picture.)

Countries with diamonds in the top right of the diagram would be classed as high-spenders/high-achievers and those in the bottom left would be low-spenders/low-achievers. Of course, it is also possible to be a low-spender/high-achiever (top left) or a high-spender/low-achiever (bottom right). If a line of best fit through these points slopes upwards, it suggests a positive association between spending per pupil (scaled by national income per head) and attainment. If the line is horizontal, it suggests that there is no association.

---

<sup>7</sup> Gordon Brown’s speech on education given at the University of Greenwich, 31 October 2007 (<http://www.number10.gov.uk/output/Page13675.asp>).

Figure 7.6. Education spending per pupil and average maths scores



Note: Canada is not shown due to lack of data.

Sources: Cumulative expenditure per student and national income per head taken from OECD, *Education at a Glance 2007* (<http://www.oecd.org/dataoecd/4/55/39313286.pdf>). Maths scores taken from OECD, *PISA 2006: Science Competencies for Tomorrow's World* (<http://www.pisa.oecd.org/dataoecd/30/17/39703267.pdf>).

The graph shows that in 2004, the UK is estimated to have spent the equivalent of two-and-a-half times its national income per head on each 5- to 16-year-old over 11 years of compulsory schooling. Pupils in the UK achieved an average maths score of 495 in 2006, placing the UK 24<sup>th</sup> out of 57 OECD and partner countries, or 17<sup>th</sup> out of the 30 OECD countries. The diamond for the UK lies above the green line of best fit, which is consistent with the UK getting slightly better 'bang for its buck' when spending on education compared with this set of countries, although some countries do much better. For example, Finland spent a similar amount to the UK across 5- to 16-year-olds (2.6 times its national income per head), but on average pupils in Finland achieved a much higher maths score, coming top of the OECD rankings.

In fact, if we look at all OECD countries together – those for which we have both spending-per-pupil data and average performance in maths – there appears to be a slight positive association between spending per pupil (scaled by national income per head) and average performance in maths (shown by the green line). However, if we exclude the two poorest countries in the OECD (Turkey and Mexico, which both had a national income per head below \$11,000 in 2005), then there is no obvious association between spending per pupil and average performance in maths (shown by the dark line). Countries with high levels of cumulative spending per pupil (scaled by national income per head), such as Italy – which spent about 3.6 times its national income per head across 5- to 16-year-olds in 2004 – appear to achieve similar results to countries that spent comparatively little, such as Greece – which spent less than twice the level of its national income per head across 5- to 16-year-olds in the same year.

Clearly, the relationship between spending per pupil and educational attainment is a complex one and it would be unwise to draw policy conclusions from a single graph.<sup>8</sup> If the UK were to reduce education spending significantly, UK students could well achieve worse results. Also, such a graph does not necessarily imply that large real increases in education spending since 1999–2000 have not improved results. However, other studies do show that the relationship between spending per pupil and attainment is at best weakly positive.<sup>9</sup>

What such results do say, however, is that higher levels of education spending are not a sufficient condition for improving educational performance. Countries such as Italy can devote large amounts of spending to education but achieve similar results to low spenders. Nor are higher levels of spending a necessary condition. Countries such as Finland can come top of the OECD rankings but still spend around the average amount per pupil.

The government is likely to meet its manifesto commitment to increase education spending as a share of national income over the course of the current Parliament, but by a smaller margin than during the previous Parliament. Moreover, it seems hard to square Gordon Brown's professed belief that industrial countries will need to increase the share of national income that they spend on education, science and innovation with the decision in the CSR to halt the rise in public spending on education as a share of national income after the increases of the past seven years. That said, there is little evidence of a reliable link between education spending and outcomes.

## Child poverty

In 1999, Tony Blair stated that 'Our historic aim will be for ours to be the first generation to end child poverty forever, and it will take a generation. It is a twenty year mission, but I believe it can be done'.<sup>10</sup> The government later clarified this pledge by stating that it aimed for the UK's child poverty rate to be among the lowest in Europe by 2020.<sup>11</sup> This was further supplemented by two intermediate targets:

- to reduce child poverty by one-quarter between 1998–99 and 2004–05;
- to reduce child poverty by one-half between 1998–99 and 2010–11.

Figures published in March 2005 revealed that the first target had been narrowly missed.<sup>12</sup> For the second target, progress will be assessed using three definitions of poverty – a relative

---

<sup>8</sup> For a more detailed discussion, see OECD, *Education at a Glance 2007*, 2007 (<http://www.oecd.org/dataoecd/4/55/39313286.pdf>).

<sup>9</sup> E. A. Hanushek, 'Measuring investment in education', *Journal of Economic Perspectives*, 1996, 10(4): 9–30.

<sup>10</sup> T. Blair, 'Beveridge re-visited: a welfare state for the 21<sup>st</sup> century' in R. Walker (ed.), *Ending Child Poverty: Popular Welfare for the 21<sup>st</sup> Century?*, Policy Press, Bristol, 1999.

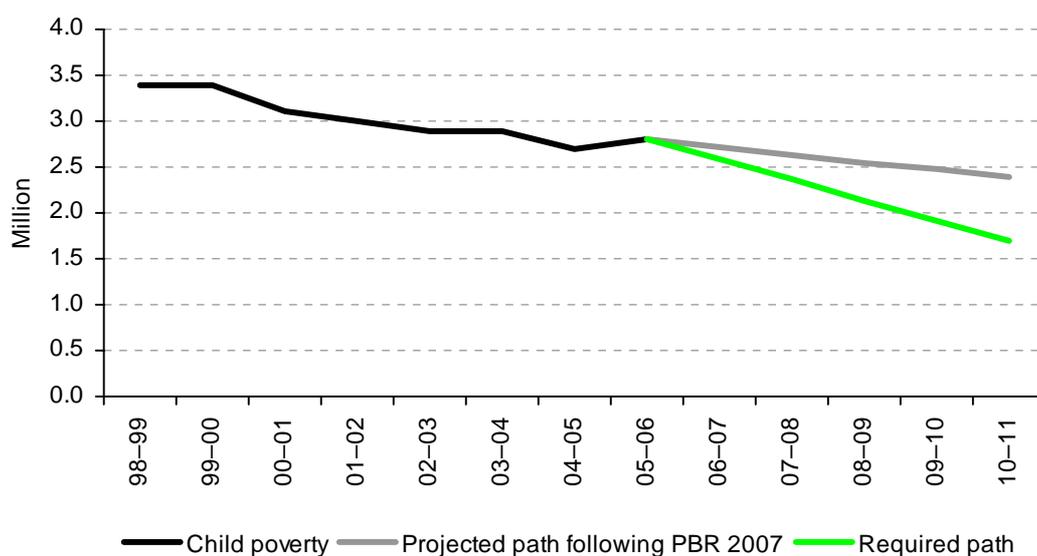
<sup>11</sup> Department for Work and Pensions, *Measuring Child Poverty*, December 2003 ([http://www.dwp.gov.uk/ofa/related/final\\_conclusions.pdf](http://www.dwp.gov.uk/ofa/related/final_conclusions.pdf)).

<sup>12</sup> Department for Work and Pensions, *Households Below Average Income 1994/95–2004/05*, Corporate Document Services, Leeds, 2006.

poverty indicator, an absolute poverty indicator and a material deprivation indicator – all of which are different from the ones used for the target for child poverty in 2004–05.<sup>13</sup>

IFS researchers have previously argued that the most binding of the government's three indicators will be the pure relative poverty indicator, which is for child poverty in the UK in 2010–11 to be one-half lower than its level in 1998–99, using a poverty line of 60% of median before-housing-costs (BHC) income and the modified OECD equivalence scale.<sup>14</sup> As shown in Figure 7.7, child poverty in the UK in 1998–99 is estimated to be 3.4 million, which means it must fall to 1.7 million in order to meet the target. The number of children in poverty in 2005–06 (the latest year for which data are available) stood at 2.8 million, having risen by 100,000 between 2004–05 and 2005–06. This means that child poverty has fallen by 600,000 (or 17.2% using rounded figures) in the seven years since 1998–99 and needs to fall by a further 1.1 million in the remaining five years between 2005–06 and 2010–11 to meet this element of the target. Thus, child poverty needs to fall by an average of over 200,000 for the next five years, having fallen by an average of less than 100,000 a year for the past seven years.

Figure 7.7. Actual, required and projected path of child poverty



Notes: Child poverty is defined as living in households in the UK with less than 60% of median BHC household income using the modified OECD equivalence scale.

Source: Authors' calculations based on the Family Resources Survey, various years. 'Projected path following PBR 2007' from an updated estimate from M. Brewer and J. Browne, 'Estimates of the costs of meeting the government's child poverty target in 2010/11: update after the Budget 2007', April 2007 ([http://www.ifs.org.uk/publications.php?publication\\_id=3973](http://www.ifs.org.uk/publications.php?publication_id=3973)).

<sup>13</sup> For more details, see HM Treasury, *PSA Delivery Agreement 9: Halve the number of children in poverty by 2010–11, on the way to eradicating child poverty by 2020*, October 2007 ([http://www.hm-treasury.gov.uk/media/B/9/pbr\\_csr07\\_psa9.pdf](http://www.hm-treasury.gov.uk/media/B/9/pbr_csr07_psa9.pdf)).

<sup>14</sup> M. Brewer, A. Goodman, J. Shaw and A. Shephard, *Poverty and Inequality in Britain: 2005*, IFS Commentary 99, March 2005 ([http://www.ifs.org.uk/publications.php?publication\\_id=3328](http://www.ifs.org.uk/publications.php?publication_id=3328)).

IFS researchers estimated in 2005 that, on unchanged policies, the number of children in poverty would fall only slightly between 2004–05 and 2010–11.<sup>15</sup> In fact, in 2005–06 the number of children in poverty actually rose by 100,000 (not a statistically significant amount). Given the tax and tax credit changes announced in the 2007 Budget and Pre-Budget Report, IFS researchers now estimate that, in the absence of further policy announcements, child poverty will be 700,000 short of the target in 2010–11 (shown by the solid grey line). To give itself a 50:50 chance of meeting the target, the government would need to spend another £3.4 billion on financial support for low-income families with children, on top of the social security and tax credit spending that it has forecast for 2010–11 in the CSR.<sup>16</sup> The extra support would need to be announced in Autumn 2009 at the latest, when the tax credit and benefit rates are set for April 2010.

## Local government

When announcing the local government settlement to Parliament in December 2007, John Healey MP, the minister for local government, said that ‘This is a tight settlement, but it is fair and it is affordable’. He also said that ‘We expect the average council tax increase in England to be substantially below 5%. We will not hesitate to use our capping powers as necessary to protect council tax payers from excessive increases’.<sup>17</sup>

This section examines whether the government might face pressure either to top up this settlement or to tolerate larger increases in council tax rates (in which case it might feel the need to offer targeted support to limit the impact on particular groups, such as pensioners).

Just how ‘tight’ is the local government settlement?

In 2006–07, local authority expenditure on services in their area accounted for around 27% of total managed expenditure (TME) by the public sector. This included spending on capital projects (e.g. roads, school buildings), spending on council housing and revenue expenditure. Revenue expenditure includes current spending on services other than council housing (e.g. schools, fire services, adult social services and the police). Revenue expenditure, which amounted to £94.0 billion in 2007–08 (nearly two-thirds of the local authority total), is the focus of this section.<sup>18</sup>

The vast majority of revenue expenditure is funded out of a combination of different grants from central government<sup>19</sup> and funds raised locally through council tax. The combination of

---

<sup>15</sup> M. Brewer, J. Browne and H. Sutherland, *Micro-Simulating Child Poverty in 2010 and 2020*, Joseph Rowntree Foundation, York, July 2006 (<http://www.jrf.org.uk/bookshop/eBooks/9781859355091.pdf>).

<sup>16</sup> An updated estimate from M. Brewer and J. Browne, ‘Estimates of the costs of meeting the government’s child poverty target in 2010/11: update after the Budget 2007’, April 2007 ([http://www.ifs.org.uk/publications.php?publication\\_id=3973](http://www.ifs.org.uk/publications.php?publication_id=3973)).

<sup>17</sup> <http://www.local.odpm.gov.uk/finance/0809/constate.pdf>.

<sup>18</sup> Figures in this paragraph from Communities and Local Government, *Local Government Finance Key Facts: England*, November 2007 (<http://www.local.odpm.gov.uk/finance/stats/keystats/key2007.pdf>) and table B6 of HM Treasury, *Public Finances Databank*, December 2007 ([http://www.hm-treasury.gov.uk/economic\\_data\\_and\\_tools/finance\\_spending\\_statistics/pubsec\\_finance/psf\\_statistics.cfm](http://www.hm-treasury.gov.uk/economic_data_and_tools/finance_spending_statistics/pubsec_finance/psf_statistics.cfm)).

<sup>19</sup> Including redistributed national non-domestic rates.

government grants is known as total aggregate external finance (AEF), which we generally refer to as the local government settlement.

On 6 December 2007, the government set out the local government settlement over the three years covered by the 2007 CSR (2008–09, 2009–10 and 2010–11). Table 7.2 shows the real-terms growth per year in this settlement (i.e. in AEF) over the whole of this period compared with that seen over spending reviews to date (1998–99 to 2007–08). It shows that over the period covered by the 2007 CSR, the local government settlement is set to increase by an average real rate of 1.5% a year. This would be less than half the growth rate over spending reviews to date. The table also shows the real-terms growth in AEF in each of the individual years covered by the CSR, which is fairly evenly spread.

**Table 7.2. Annual increases in grants to local authorities and in council tax**

	<b>Reviews to date (1998–99 to 2007–08)</b>	<b>CSR 2007 (2007–08 to 2010–11)</b>	<b>2007–08 to 2008–09</b>	<b>Of which: 2008–09 to 2009–10</b>	<b>2009–10 to 2010–11</b>
Local government settlement (AEF)	+4.2%	+1.5%	+1.3%	+1.6%	+1.6%
<i>Of which:</i>					
Special grants	Not comparable	+1.8%	+1.2%	+2.2%	+2.1%
Main grant	Not comparable	+0.3%	+0.9%	+0.1%	–0.1%
<i>Assuming cash increase in council tax rates of 5% a year over CSR period:</i>					
Council tax rates	+3.9%	+2.2%			
Council tax revenues	+4.8%	+3.1%			

Notes: Increases in council tax rates and council tax revenues for CSR 2007 refer to maximum potential real increases given a maximum cash-terms increase of 5.0%. Due to the introduction of the Dedicated Schools Grant in 2006–07 (moving funding for schools from the main grant to a special ring-fenced grant), we do not present the increase in special grants over spending reviews to date.

Sources: Communities and Local Government, *Local Government Finance Key Facts: England*, November 2007 (<http://www.local.odpm.gov.uk/finance/stats/keystats/key2007.pdf>); 2008/09 *Local Government Settlement Consultation* (<http://www.local.communities.gov.uk/finance/0809/grant.htm#con089>); deflators taken from HM Treasury website ([http://www.hm-treasury.gov.uk/economic\\_data\\_and\\_tools/gdp\\_deflators/data\\_gdp\\_index.cfm](http://www.hm-treasury.gov.uk/economic_data_and_tools/gdp_deflators/data_gdp_index.cfm)); Local Government Association, *Local Government Finance Settlement 2008–09 to 2010–11*, Briefing, December 2007 (<http://www.lga.gov.uk/lga/aio/103566>); authors' calculations.

Is such a slowdown in the local government settlement feasible, given that the government has stated that it expects the average increases to be 'substantially below 5%' and that it will use its capping powers to 'protect council tax payers from excessive increases'?

Given that the government desires an average increase 'substantially' below 5% in cash terms, let us assume that the maximum average increase in council tax rates in cash terms that it intends to permit is 5%. This is equivalent to a maximum average increase of 2.2% a year in real terms, after accounting for expected inflation between 2007–08 and 2010–11. But this would not necessarily imply that the maximum real-terms increase in council tax revenues over this period would be 2.2% per year, as demographic trends will also affect changes in council tax revenues. We estimate that if the trends in the underlying council tax base follow the pattern seen over the last 10 years, council tax revenues would grow by 3.1% per year in

real terms.<sup>20</sup> This is lower than the 4.8% a year real increase delivered over spending reviews to date, as is shown in Table 7.2. This implies that central government intends that the two main sources of funding for revenue expenditure – council tax and grants from central government – should both grow much less quickly over the CSR period than they did under the previous reviews.

The slowdown looks even more dramatic when we remove special grants from the settlement. Most of these are ring-fenced for specific items. (The largest is the Dedicated Schools Grant, all of which must be spent on schools.) These special grants are set to grow by an average of 1.8% per year in real terms, leaving the remaining ‘main grant’ to grow by only 0.3% per year on the same basis, a near real-terms freeze. Moreover, much of this growth is planned for 2008–09. A real-terms cut is planned for 2010–11. The extent to which this will restrict councils’ ability to increase spending on areas covered by the main grant will depend on the extent to which councils currently top up spending on areas covered by special grants from council tax revenues.

The local government settlement looks particularly tight over the next few years. Pressures are likely to be particularly acute in 2009–10 and 2010–11, given the spread of real-terms increases in the main grant shown in Table 7.2. As a result, local authorities may not be happy to keep council tax increases ‘substantially below 5%’ as the government wishes.

This could confront the government with a set of unpalatable choices:

- cap the authorities and risk taking the blame for the consequences to public services;
- cap the authorities but allow them to raise extra revenue by increasing user charges, sales and fees;
- top up the overall local government settlement;
- allow local authorities to raise council tax more than the desired amount, perhaps with additional targeted support to protect specific groups such as pensioners.

## Defence

In November 2007, a number of former defence chiefs criticised the recent CSR settlement for defence spending.<sup>21</sup> We do not have the expertise to judge whether they are correct, but we can assess whether the defence settlement is relatively tight in historical terms.

---

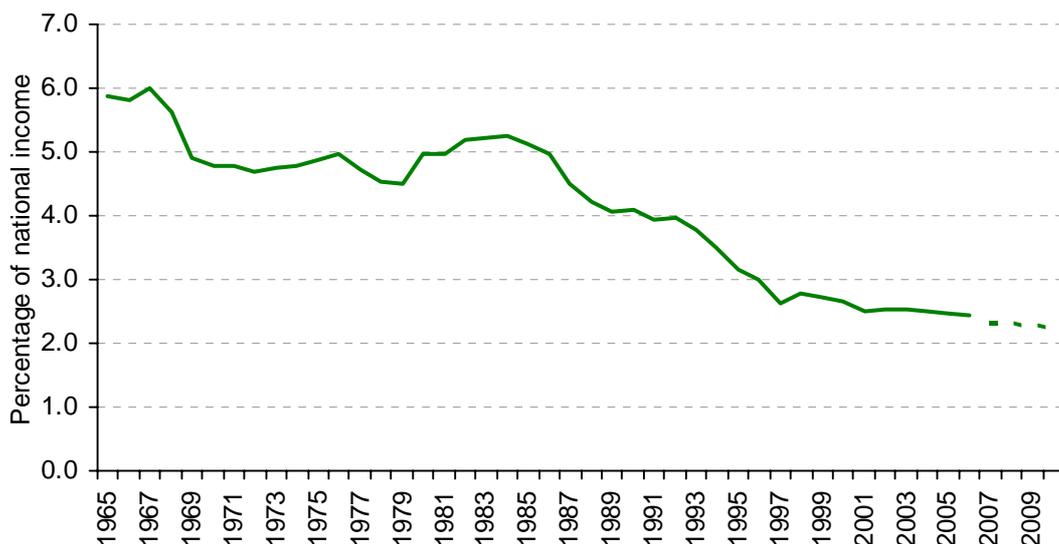
<sup>20</sup> The growth in the revenue obtained from council tax will depend upon changes in other factors. For instance, it depends on the growth in the number of households, changing residency patterns across council tax bands, average size of households, number of second homes and many other factors. Since 1998–99, growth in council tax revenues has outstripped the growth in average rates of council tax. On average, the annual growth in council tax revenues has exceeded growth in council tax rates by 0.9 percentage points over spending reviews to date (i.e. between 1998–99 and 2007–08). In other words, this suggests that if councils had chosen to freeze council tax rates in real terms, then council tax revenues would still have grown by an average of 0.9% per year in real terms. If we assume that this average excess growth in revenues is maintained over the period covered by the 2007 Comprehensive Spending Review, then if all councils increase their Band D rates by an annualised average of 2.2% per year in real terms (5% in cash terms), council tax revenues would grow by an annualised average of 3.1% in real terms.

<sup>21</sup> ‘Retired military chiefs join forces to battle for a bigger war chest’, *The Times*, 9 November 2007 (<http://www.timesonline.co.uk/tol/news/politics/article2836430.ece>).

If the CSR plans for defence spending are delivered as planned, then defence spending will grow by an average of 1.5% per year in real terms between 2007–08 and 2010–11. This is slightly higher than the average delivered under Labour to date of 1.3% per annum.

Figure 7.8 shows the share of national income devoted to defence spending in a longer historical context, together with the plans through to 2010–11. It shows that between the late 1960s and late 1970s, defence spending hovered just below 5% as a share of national income. It then rose as a share of national income up to 1985, following a NATO agreement in 1977<sup>22</sup> signed by the then Labour government to increase defence spending by 3% per year in real terms over the following seven years (which was kept to by the incoming Conservative administration in 1979). Following the end of this agreement, between the mid-1980s and mid-1990s there was a substantial fall in the share of national income devoted to defence spending, declining from 5.3% in 1984 to reach 2.6% in 1997. Since Labour came to power in 1997, the share has continued to decline, though at a much slower rate. If plans for the period covered by the CSR are delivered, then defence spending is expected to represent 2.3% of national income in 2010–11, which would be the lowest level seen over the last fifty years.

Figure 7.8. UK defence spending since 1965



Notes: Calendar years up to 1997; national income created as weighted average of financial years. Financial years thereon.

Sources: Defence spending from ONS *Blue Book* 1979 to 1997, PESA COFOG 1996–97 to 2006–07 and CSR 2007–08 to 10–11; GDP from HM Treasury website.

The decline in defence spending to date under Labour is much less dramatic than the decline between the mid-1980s and mid-1990s, and the planned decline for the next three years is slightly slower than that delivered by Labour over the last 10 years. However, it should be said that the decline in defence spending over the early 1990s partly reflects the fact that the end of the cold war reduced the UK’s military commitments. The key question is whether or not the CSR settlement for defence is likely to prove commensurate with current and future demands on the armed forces. This is a question that we cannot even begin to answer, but the

<sup>22</sup> <http://www.nato.int/docu/comm/49-95/c770517b.htm>.

former defence chiefs do not believe it to be likely. For instance, former Chief of the Defence Staff, Lord Boyce, said that:

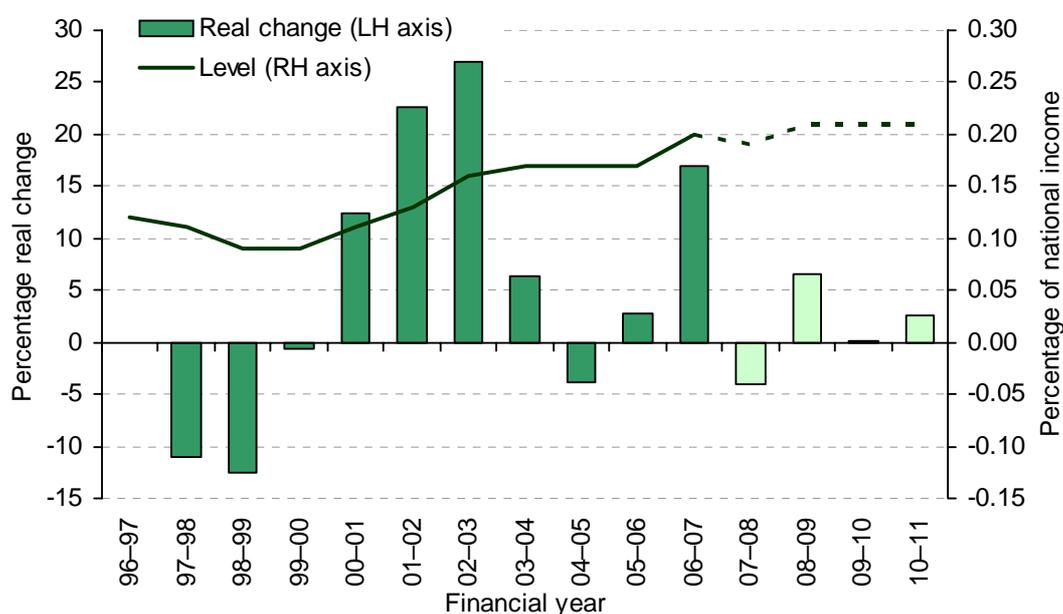
Even though defence did see an increase in the most recent comprehensive spending review, that goes nowhere near addressing the fundamental issue of proper funding and over-commitment.

## Transport

Transport spending has been historically volatile, with a comparatively low base that can be significantly affected by major infrastructure projects in a particular year. Figure 7.9 shows the uneven path of transport spending since 1996–97: real spending cuts in Labour’s first three years were followed by three years of rapid growth. Since 2003–04, the trend in transport spending has been less clear, with real cuts in some years (2004–05, 2007–08) and strong growth in others. If current plans are delivered, by 2010–11 transport spending will have more than doubled as a proportion of national income, from its recent low point of 0.09% of national income in 1999–2000 to more than 0.2% at the end of the CSR period.

Citing the long-term nature of transport planning, in 2000 the government published a ‘Ten-Year Plan’ for transport policy,<sup>23</sup> which set out guideline funding allocations for public

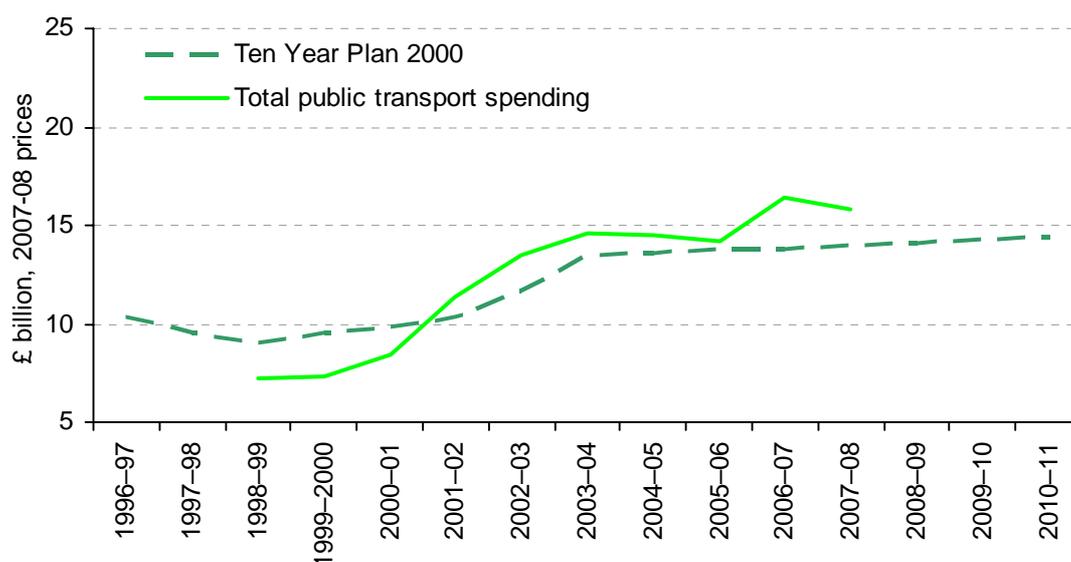
Figure 7.9. Transport spending



Note: Figures refer to public sector transport spending based on the UN Classification of the Functions of Government (COFOG), the international standard, as used in the Public Expenditure Statistical Analysis. Source: Period to 2006–07 from HM Treasury, *Latest Functional Data*, October 2007 ([http://www.hm-treasury.gov.uk/media/6/1/PBR\\_2007\\_functional\\_series.xls](http://www.hm-treasury.gov.uk/media/6/1/PBR_2007_functional_series.xls)). Period from 2007–08 onwards from table D7 of HM Treasury, *2007 Pre-Budget Report and Comprehensive Spending Review*, October 2007 ([http://www.hm-treasury.gov.uk/media/9/7/pbr\\_csr07\\_annexd3\\_199.pdf](http://www.hm-treasury.gov.uk/media/9/7/pbr_csr07_annexd3_199.pdf)). This assumes real growth in national income of 2½% per year, the Treasury’s ‘cautious’ assumption for real GDP growth used for its public finance projections.

<sup>23</sup> Department for Transport, *Transport Ten Year Plan 2000* (<http://www.dft.gov.uk/about/strategy/whitepapers/previous/transporttenyearplan2000>).

Figure 7.10. Department for Transport budget compared with Ten Year Plan



Sources: Table A.3 of Department for Transport, *Transport Ten Year Plan 2000* (<http://www.dft.gov.uk/about/strategy/whitepapers/previous/transporttenyearplan2000>); Department for Transport Annual Reports, 2004 to 2007 (<http://www.dft.gov.uk/about/publications/apr/>).

spending on transport through to 2010–11. Figure 7.10 compares the public transport spending envisaged by this 10-year plan with actual public transport spending up to 2007–08. It is clear that from 2001–02 onwards, the government decided to spend slightly more on transport than the 10-year plan published in 2000 indicated.

The 10-year funding guideline was extended to 2018–19 in the 2007 CSR. It indicated that the Department for Transport (DfT) can plan for increases in its programme budget of 2¼% a year in real terms from 2011–12 to 2018–19.<sup>24</sup> This would represent a step down in real transport spending growth when compared with the 4.3% average annual growth delivered by Labour to date. Moreover, the Crossrail project – a cross-London rail link for which £5 billion of public funding was agreed in 2007, and whose construction is due to begin in 2010 – looks set to take up the majority of DfT’s funding increase for the years 2010–11 to 2012–13.<sup>25</sup>

Of the real funding increase planned for the DfT from 2014 to 2019, however, about £20 billion cumulatively over those six years is currently unallocated. DfT has discussed possible uses for the money in its recent long-term strategy document, *Towards a Sustainable Transport System*,<sup>26</sup> with ultra-long trains on a new London–Birmingham–Manchester line, expanded congestion charging schemes and widening motorways among the options being debated.<sup>27</sup>

<sup>24</sup> HM Treasury, *2007 Pre-Budget Report and Comprehensive Spending Review*, October 2007 ([http://www.hm-treasury.gov.uk/media/9/7/pbr\\_csr07\\_annexd3\\_199.pdf](http://www.hm-treasury.gov.uk/media/9/7/pbr_csr07_annexd3_199.pdf)).

<sup>25</sup> See page 45 of Department for Transport, *Towards a Sustainable Transport System*, October 2007 (<http://www.dft.gov.uk/about/strategy/transportstrategy/pdfsustaintranssystem.pdf>).

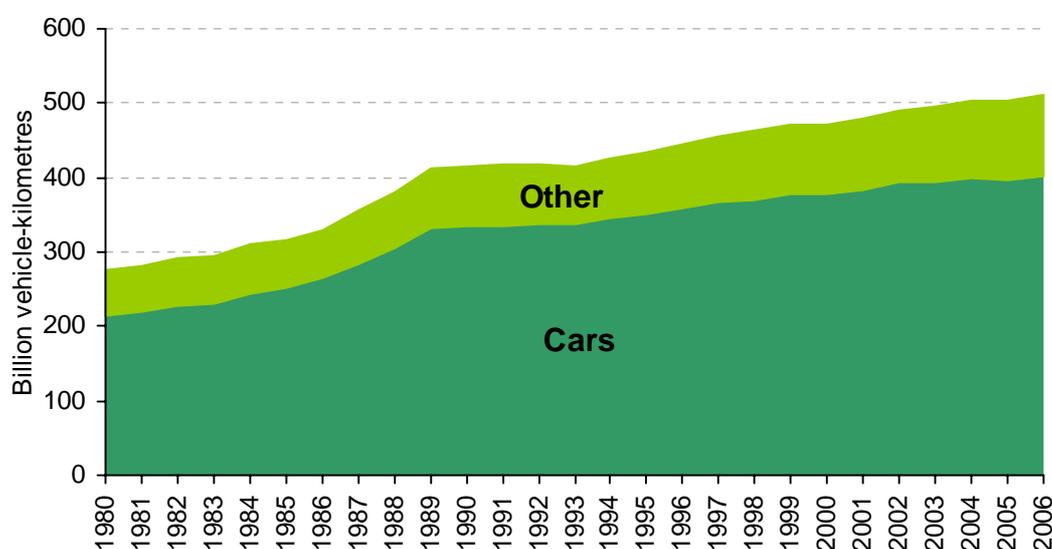
<sup>26</sup> Department for Transport, *Towards a Sustainable Transport System*, October 2007 (<http://www.dft.gov.uk/about/strategy/transportstrategy/pdfsustaintranssystem.pdf>).

<sup>27</sup> See, for example, ‘Radical transport options unveiled’, *Financial Times*, 29 October 2007.

UK transport policy has been the subject of a series of ambitious government targets – ambitions that have rarely been met. New targets were introduced in the 2004 Spending Review, this time in the form of seven Public Service Agreement (PSA) targets for the DfT, ranging from reducing road congestion to increasing bus and light-rail use. However, the House of Commons Transport Committee’s annual report for 2006–07<sup>28</sup> found that the DfT was on track to meet only two of these seven targets – on road safety and rail punctuality. Targets on congestion, bus use, air quality and climate change were all set to be missed.

Figure 7.11 shows perhaps the single most significant trend facing transport policymakers – the relentless rise in road traffic, and car use in particular. Total road traffic increased by 84% between 1980 and 2006, from 277 to 511 billion vehicle-kilometres. The majority of the growth was in car traffic, which rose by 87% over the same period.

Figure 7.11. Road traffic, 1980 to 2006

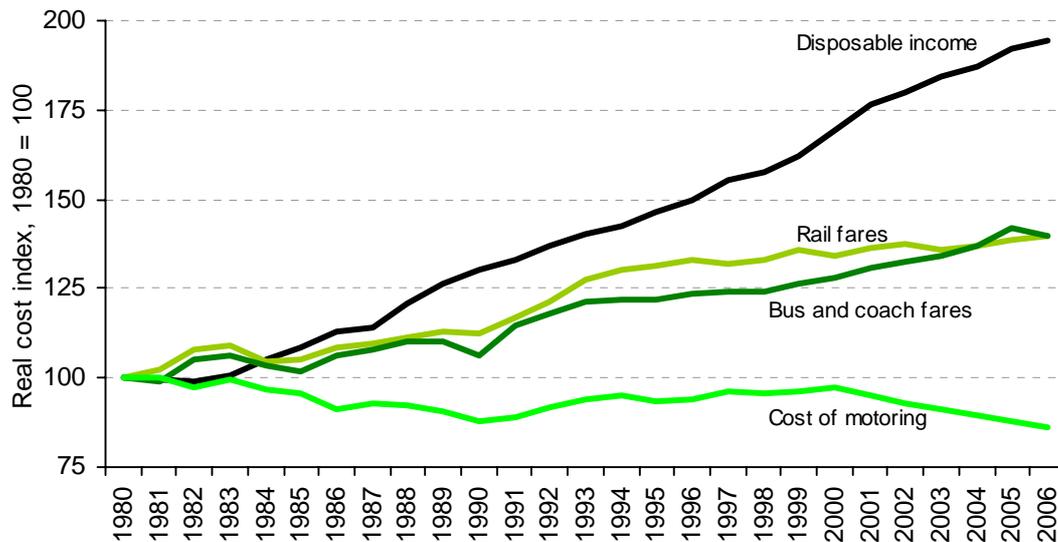


Note: 'Other' category includes light vans, motorcycles, pedal cycles, heavy goods vehicles, buses and coaches.  
 Source: Trend 1.1a of Department for Transport, *Transport Trends 2007*  
[\(http://www.dft.gov.uk/pgr/statistics/datatablespublications/trends/current/\)](http://www.dft.gov.uk/pgr/statistics/datatablespublications/trends/current/).

Figure 7.12 illustrates one important factor behind this increase in car use: the cost of motoring has fallen by over 13% in real terms since 1980 (despite recent increases in the cost of petrol and diesel), while disposable incomes have almost doubled in real terms over the same period. Bus and coach fares have risen by about 40% in real terms since 1980, while rail fares have risen by the same proportion. Thus while all modes of transport have become more affordable since 1980, it is private motoring that has seen the biggest increase in affordability. This increased affordability has been reflected in trends in car ownership: in 1980 only 59% of households had access to a car, while by 2005 over 75% of households did (with 31% of households having access to two or more cars).

<sup>28</sup> House of Commons Transport Committee, *Department for Transport Annual Report 2006*, February 2007  
<http://www.publications.parliament.uk/pa/cm200607/cmselect/cmtran/95/95.pdf>.

Figure 7.12. Changes in the real cost of transport and income



Note: Overall cost of motoring index includes purchase, maintenance, petrol and oil, and tax and insurance.

Source: Trend 2.6 of Department for Transport, *Transport Trends 2007*

(<http://www.dft.gov.uk/pgr/statistics/datatablespublications/trends/current/>).

Meeting the government's transport targets is likely to require more than simply spending money. Ultimately, if the government is to meet its targets (on road congestion in particular), it will need to change people's behaviour, by changing the prices individuals face when they consider making a journey. The importance of 'getting the prices right' across different modes of transport was particularly emphasised in the 2006 Eddington Study of transport policy, commissioned jointly by the Treasury and DfT. The study recommends a targeted approach focused on the most congested, crowded and unreliable parts of the UK's travel networks, and highlights the importance of sending the right price signals to travellers. In particular, it argues that 'the potential for benefits from a well-designed, large-scale road pricing scheme is unrivalled by any other intervention'.<sup>29</sup>

In its response to the Eddington Study, the Department for Transport has signalled willingness to support local road pricing schemes (Greater Manchester and Cambridge have already submitted proposals), but states that introducing road pricing on national networks 'is a decision for the future'.<sup>30</sup> Recent history suggests, however, that without grasping the nettle of road pricing, the government's transport spending may do little to check increasing road traffic.

## International aid

The year 2007 marked the midway point in efforts to achieve the UN's Millennium Development Goals – eight internationally agreed targets set out in the UN's Millennium Declaration, ranging from halving extreme poverty to halting the spread of HIV/AIDS by

<sup>29</sup> Page 39 of the executive summary of HM Treasury, *The Eddington Transport Study*, December 2006 (<http://www.dft.gov.uk/162259/187604/206711/executivesummary>).

<sup>30</sup> Page 49 of Department for Transport, *Towards a Sustainable Transport System*, October 2007 (<http://www.dft.gov.uk/about/strategy/transportstrategy/pdfsustaintranssystem.pdf>).

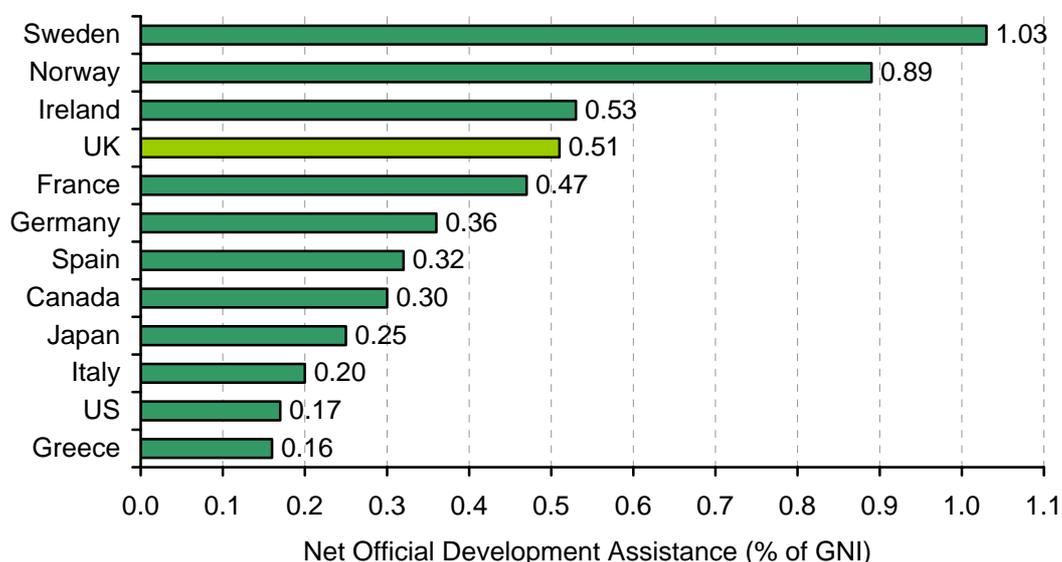
2015.<sup>31</sup> Having signed up to these goals in the year 2000, the UK government has made several concrete spending pledges, including commitments on education (where DfID has committed to spend £8.5 billion by 2015) and health (where DfID has committed £1 billion between 2007 and 2015 to the Global Fund to Fight AIDS, Tuberculosis and Malaria).<sup>32</sup>

Under plans set out in the 2007 CSR, the Department for International Development (DfID) budget is set to grow faster than government spending as a whole over the CSR period. With average planned real increases of 10.9% per year between 2007–08 and 2010–11, the DfID budget is set to reach more than £7 billion (at current prices) by 2010–11.

The 2007 CSR also reiterated the government’s commitment to achieve the UN’s target of 0.7% of gross national income (GNI) spent on Official Development Assistance (ODA). While EU countries have set a target of reaching the 0.7% mark by 2015, Labour’s 2005 election manifesto set a timetable for meeting this level two years earlier, in 2013. Figure 7.13 shows that the UK’s ODA spending in 2006 (as a percentage of GNI) compared favourably with those of many other developed countries, with the notable exceptions of Sweden and Norway.

However, Figure 7.13 gives a slightly misleading picture of the UK’s relative standing, as ODA figures in 2006 (and 2005) were distorted by the inclusion of large one-off debt write-offs to less developed countries – notably Nigeria and Iraq – in these years. To gain a clearer picture of trends in UK aid spending, Figure 7.14 shows ODA as a percentage of GNI since 2001, along with projections up to the end of the 2007 CSR period in 2010–11 if plans going forward are delivered in full.

Figure 7.13. Official Development Assistance (% of GNI, 2006)

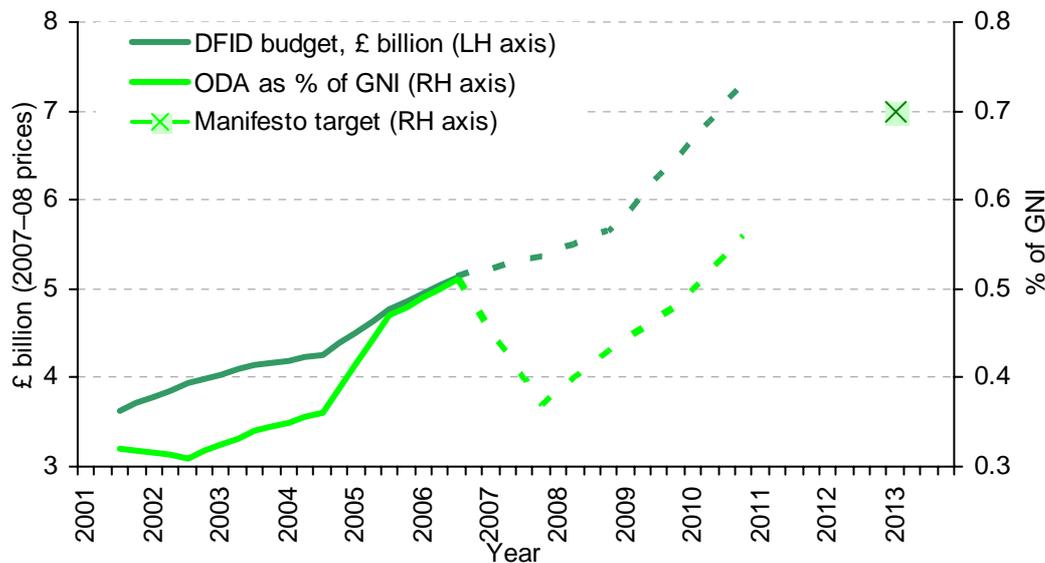


Source: Table 8 of Department for International Development, *Statistics on International Development*, October 2007 (<http://www.dfid.gov.uk/Pubs/files/sid2007/tables-index.asp>).

<sup>31</sup> More information about the Millennium Development Goals is available at <http://www.un.org/millenniumgoals/>.

<sup>32</sup> Page 237 of HM Treasury, *2007 Pre-Budget Report and Comprehensive Spending Review*, October 2007 ([http://www.hm-treasury.gov.uk/media/6/B/pbr\\_csr07\\_annexd10\\_148.pdf](http://www.hm-treasury.gov.uk/media/6/B/pbr_csr07_annexd10_148.pdf)).

Figure 7.14. Official Development Assistance and the Department for International Development budget



Note: ODA series up to 2006 is based on calendar-year data from DfID, while projections from 2007–08 onwards are based on financial-year data from HM Treasury, with linear interpolation used between data points.

Sources: DfID budget to 2006–07 from HM Treasury, *Public Expenditure Statistical Analyses*, April 2007 ([http://www.hm-treasury.gov.uk/media/1/A/pesa2007\\_c1tables.xls.xls](http://www.hm-treasury.gov.uk/media/1/A/pesa2007_c1tables.xls.xls)). ODA to 2006 from table 7 of DfID, *Statistics on International Development 2007*, October 2007 (<http://www.dfid.gov.uk/pubs/files/sid2007/contents.asp>). DfID budget and ODA from 2007–08 onwards from tables C16 and D17 of HM Treasury, *2007 Pre-Budget Report and Comprehensive Spending Review*, October 2007 ([http://www.hm-treasury.gov.uk/media/6/B/pbr\\_csr07\\_annexd10\\_148.pdf](http://www.hm-treasury.gov.uk/media/6/B/pbr_csr07_annexd10_148.pdf)).

The effect of the debt write-offs in 2005 and 2006 can be clearly seen, as they push the UK's ODA up to over 0.5% of GNI in 2006. Such large debt write-offs are not due to be repeated in future years, however, and so ODA as a percentage of GNI falls markedly in 2007–08. Nonetheless, were the planned trend in ODA growth from 2007–08 to 2010–11 to continue, the government would meet its manifesto pledge to reach the UN target of 0.7% of GNI by 2013. It would, though, cost another 0.15% of national income over a two-year period in which the Treasury is currently projecting that total public spending will fall by 0.2% of national income.

Figure 7.14 also shows the overall DfID budget (which is not distorted by debt write-offs) to make clear that the fall in ODA in 2007 does not represent a cut in government spending on international development. In fact, total overseas aid is set to grow even faster than the DfID budget – by as much as 17% a year over the CSR period to 2010–11 – as aid is channelled through other government departments as well as DfID.<sup>33</sup> Funds newly established in the 2007 CSR will distribute aid money through the Department for the Environment, Food and Rural Affairs (DEFRA), the Ministry of Defence (MoD) and the Foreign and Commonwealth Office (FCO), as well as through DfID directly.

Overall, then, current plans make the government well-placed to meet its commitments on international aid through to 2013. But this will require more resources during the next

<sup>33</sup> See, for example, 'Spending Review: Treasury to meet aid pledges', *Financial Times*, 10 October 2007.

spending review, a period over which the Treasury expects to continue cutting spending overall as a share of national income.

## 7.4 Conclusion

On average, public spending is set to increase by 2.1% per year in real terms over the period covered by the 2007 CSR, cutting public spending as a proportion of national income from 42.0% in 2007–08 to 41.6% by 2010–11. This compares with a rise from 37.0% in 1999–2000 to 42.0% by 2007–08. The government has a number of goals and objectives it has set itself over this period and beyond. Are the planned increases in public spending likely to be sufficient to meet these goals and objectives, or will the government need to top up these spending plans or rein back its policy goals?

There is one area of spending where the government is certainly on course to meet its commitments:

- International development has enjoyed the biggest spending increases of any department under Labour and will continue to do so under the CSR. The government is also on course to meet its commitment to increase Official Development Assistance to the 0.7% of GNI recommended by the UN. To do so will require an additional 0.15% of national income in the next spending review, tightening the likely pressures elsewhere.

There are a number of areas where there is considerable uncertainty over whether planned spending increases alone will allow the government to achieve all its objectives:

- The government is likely to meet its manifesto commitment to increase public spending on education as a share of national income during this Parliament. But the share is not set to increase over the CSR period, even though Gordon Brown says that public and private spending on education, science and innovation needs to increase significantly. However, it is not clear that high education spending is sufficient or necessary to achieve ‘world-class’ results.
- The government looks unlikely to meet its medium-term goals with regard to transport policy, though it has promised real-terms increases in transport spending of at least 2¼% up to 2017. Higher public spending is unlikely to do much to achieve the goal of reducing traffic, as motoring has been becoming increasingly affordable over time.
- The government currently plans to increase defence spending by 1.5% in real terms per year over the CSR period. This is slightly higher than the 1.3% it has delivered to date, but former defence chiefs have argued that this is too little to meet the military’s needs.

In other areas, there is considerable evidence to suggest that spending plans would need to be topped up to avoid government objectives being missed:

- The government looks unlikely to meet its target to halve child poverty between 1998 and 2010, unless it is able to find £3.4 billion of extra money to increase support for families with children above that assumed in public finance forecasts.
- The local government settlement between 2008 and 2010 looks particularly tight, with little scope to increase spending on local services, given the prospect of ‘capping’ for

councils that propose cash-terms increases in council tax rates above 5%. The pressures could be particularly severe in 2010–11, when the main grant is to be cut in real terms.

- Notwithstanding the rapid increases of the past seven years, the amount spent on the NHS has fallen short of that recommended by Sir Derek Wanless to achieve a world-class service. The CSR settlement for health, while more generous than that for most departments, would, if delivered, exacerbate this shortfall.