

Institute for Fiscal Studies



Risks to spending

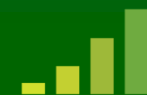
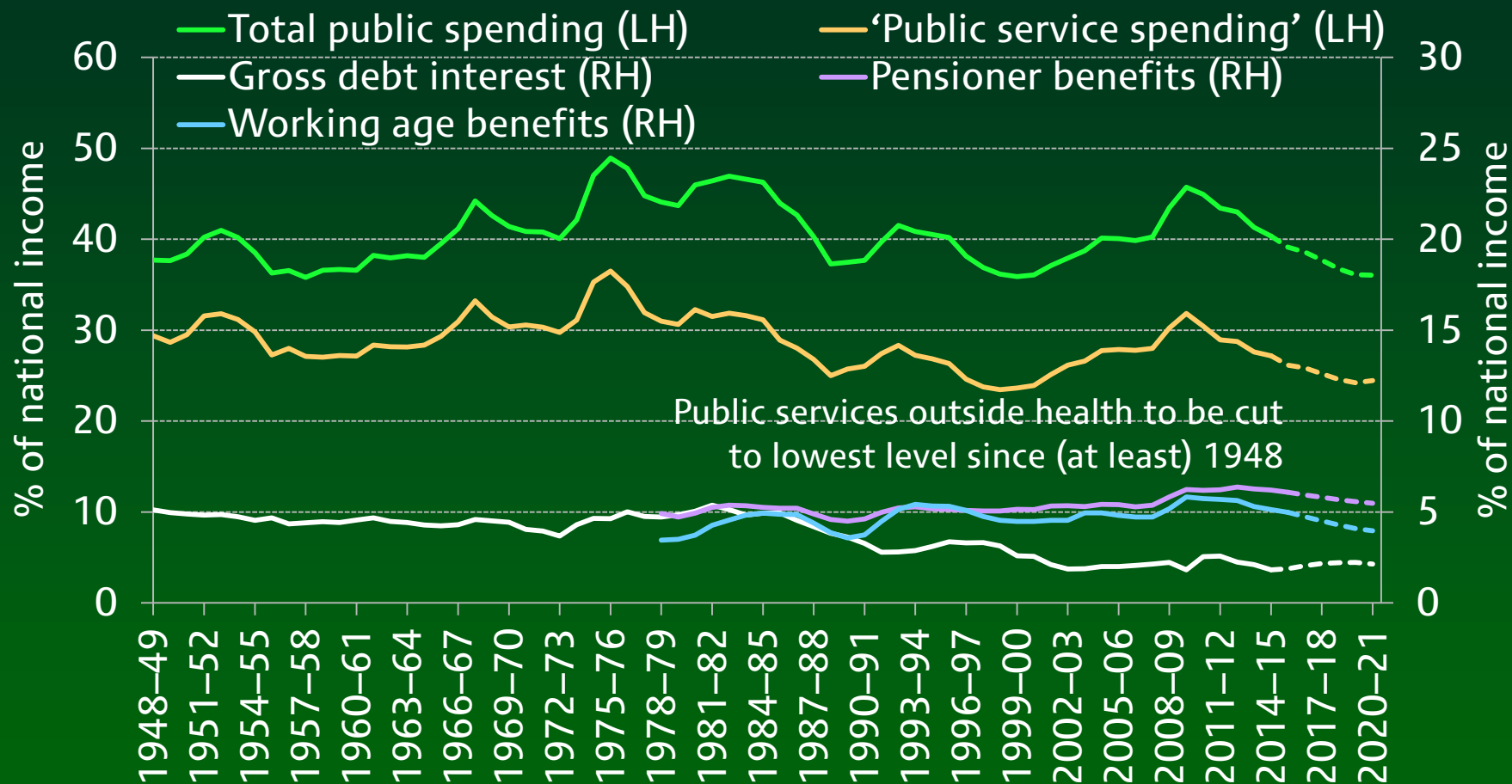
Gemma Tetlow

@TheIFS

#IFSGB2016



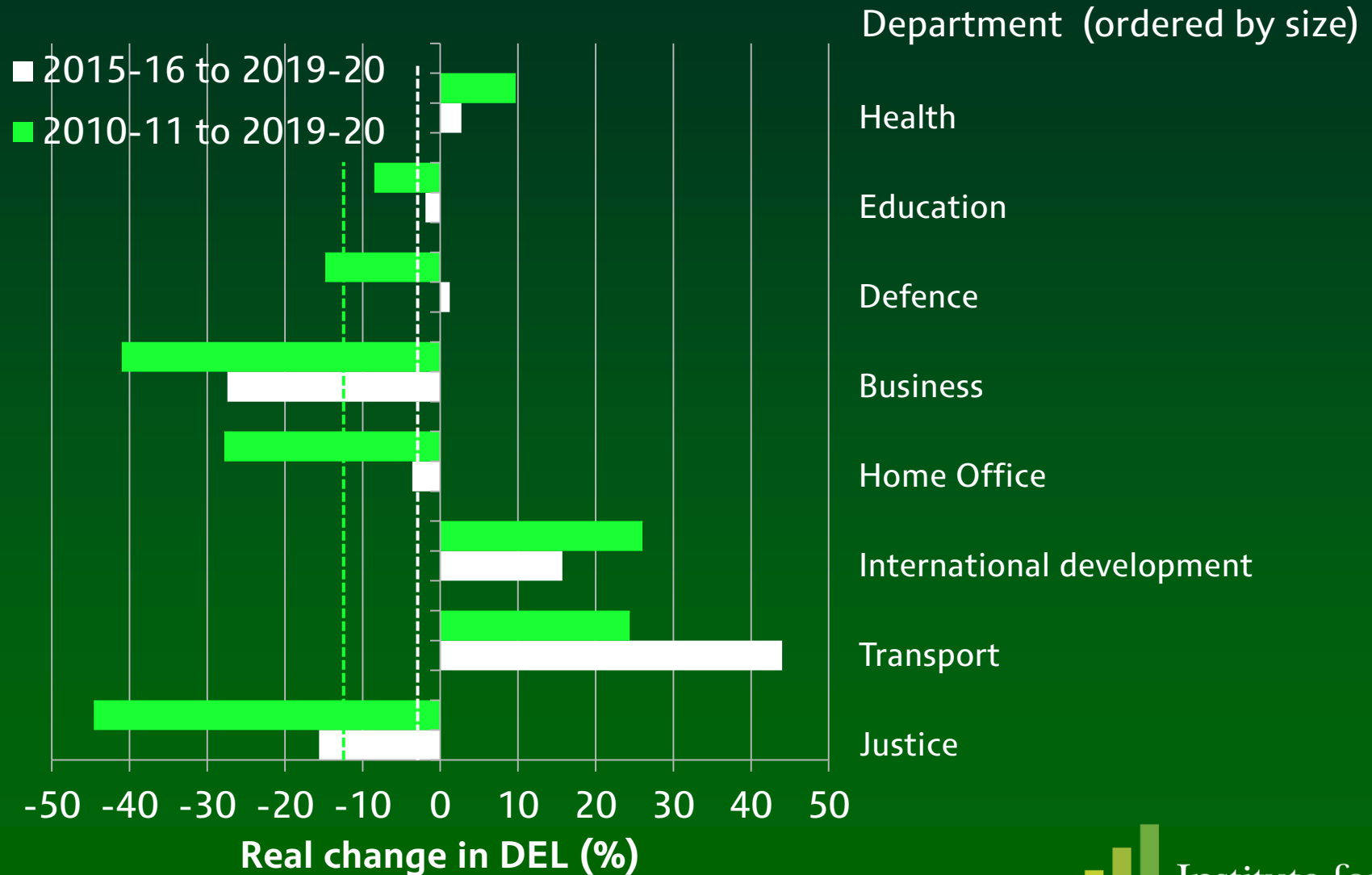
Public spending to fall to a low level by historical standards



Spending on public services set to see further significant cuts

- Departmental spending by central government
 - to be cut by 2.3% in real terms between 2015–16 and 2019–20
 - on top of 10.4% cut already seen since 2010–11
 - average cut per year (0.6%) to be slower than since 2010–11 (2.2%)

Changes in departmental spending: over 4 years and over 9 years



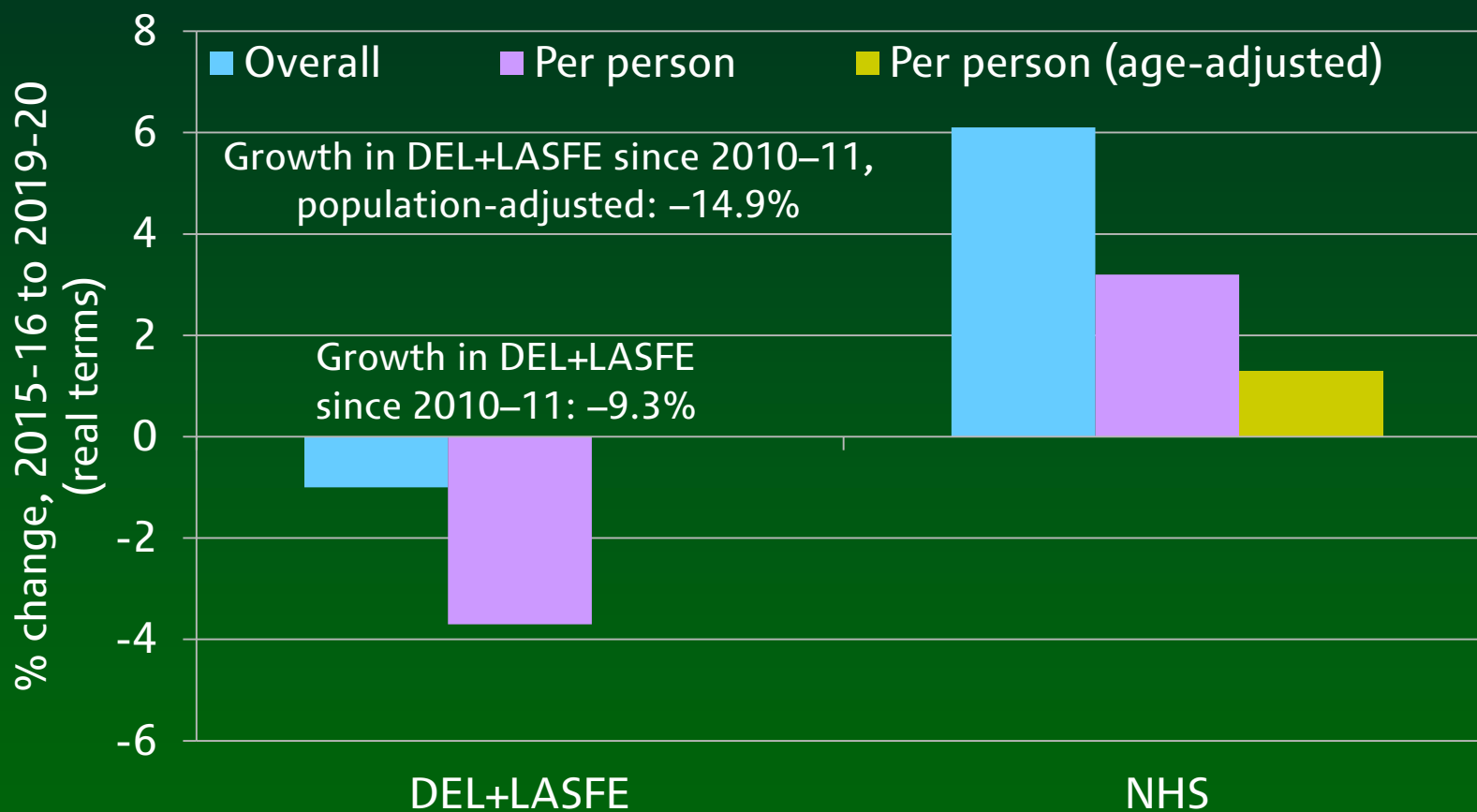
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 - average cut per year (0.6%) to be slower than since 2010–11 (2.2%)
- Some public services also financed through locally-raised revenues: including these revenues, cuts look smaller
 - DEL+LASFE to be cut by 1.0% over next four years
 - on top of 8.3% cut already seen since 2010–11

Can these plans be delivered?

- Cuts over next 4 years significantly slower than over last 5 years
- Since 2010–11, departments have underspent their allocated budgets
 - OBR's current borrowing forecast assumes they continue to do so (e.g. £4 billion in 2019–20)
- Risks
 - likely that cuts that were easy to identify and deliver were made first
 - rising demand for public services

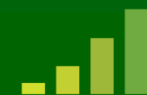
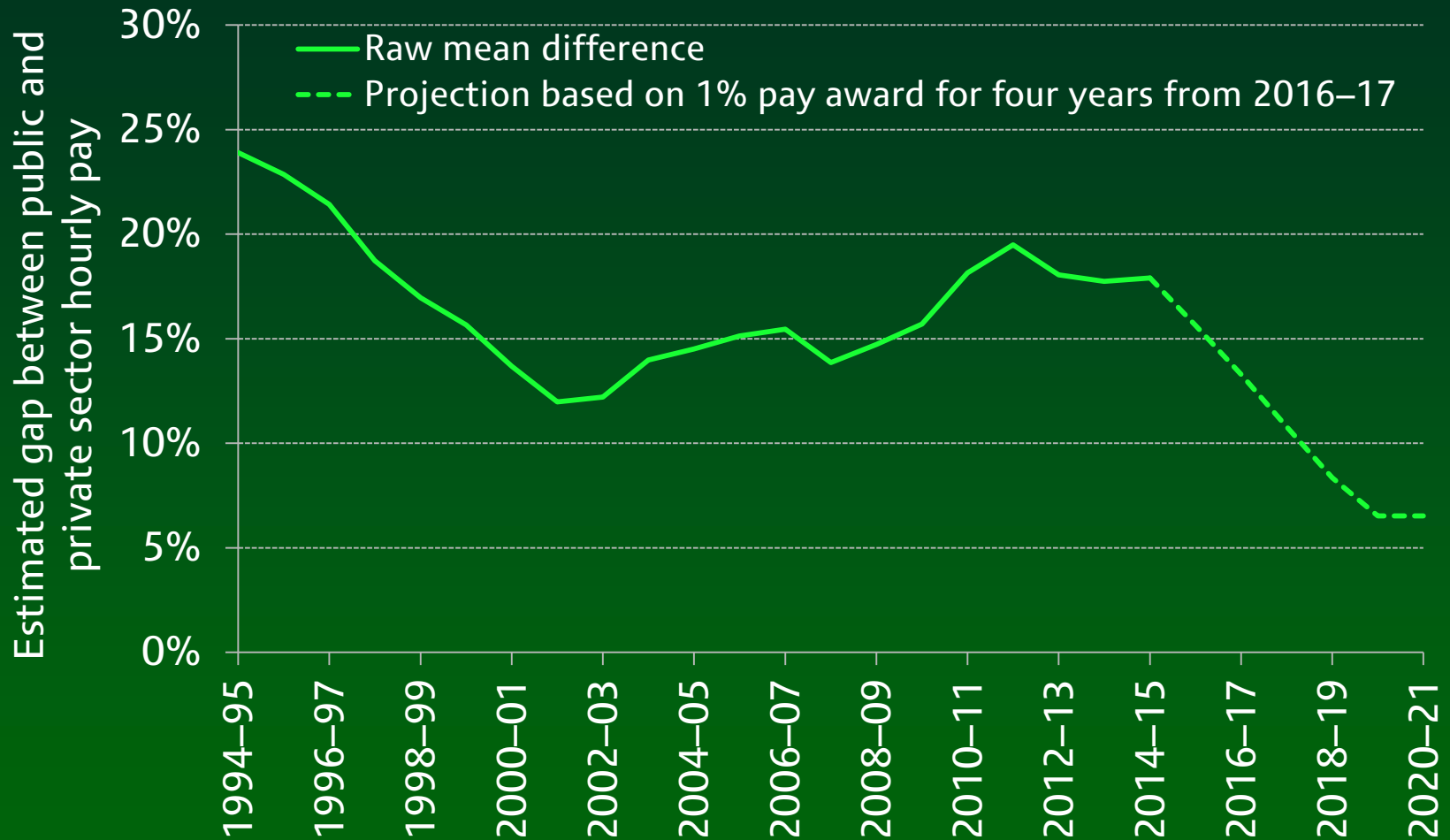
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 - rising demand for public services
 - recruitment and retention of adequately motivated, sufficiently high quality staff

Squeezing public spending by holding down public sector wages



Other risks: additional costs of employment

- In 2016–17, contracting out for defined benefit schemes ends
 - increases employees' NICs: up to £480 per year
 - estimated total cost to public sector employers: £3.3 billion
- Other pressures
 - National Living Wage
 - apprenticeship levy
 - requirement to hire apprentices

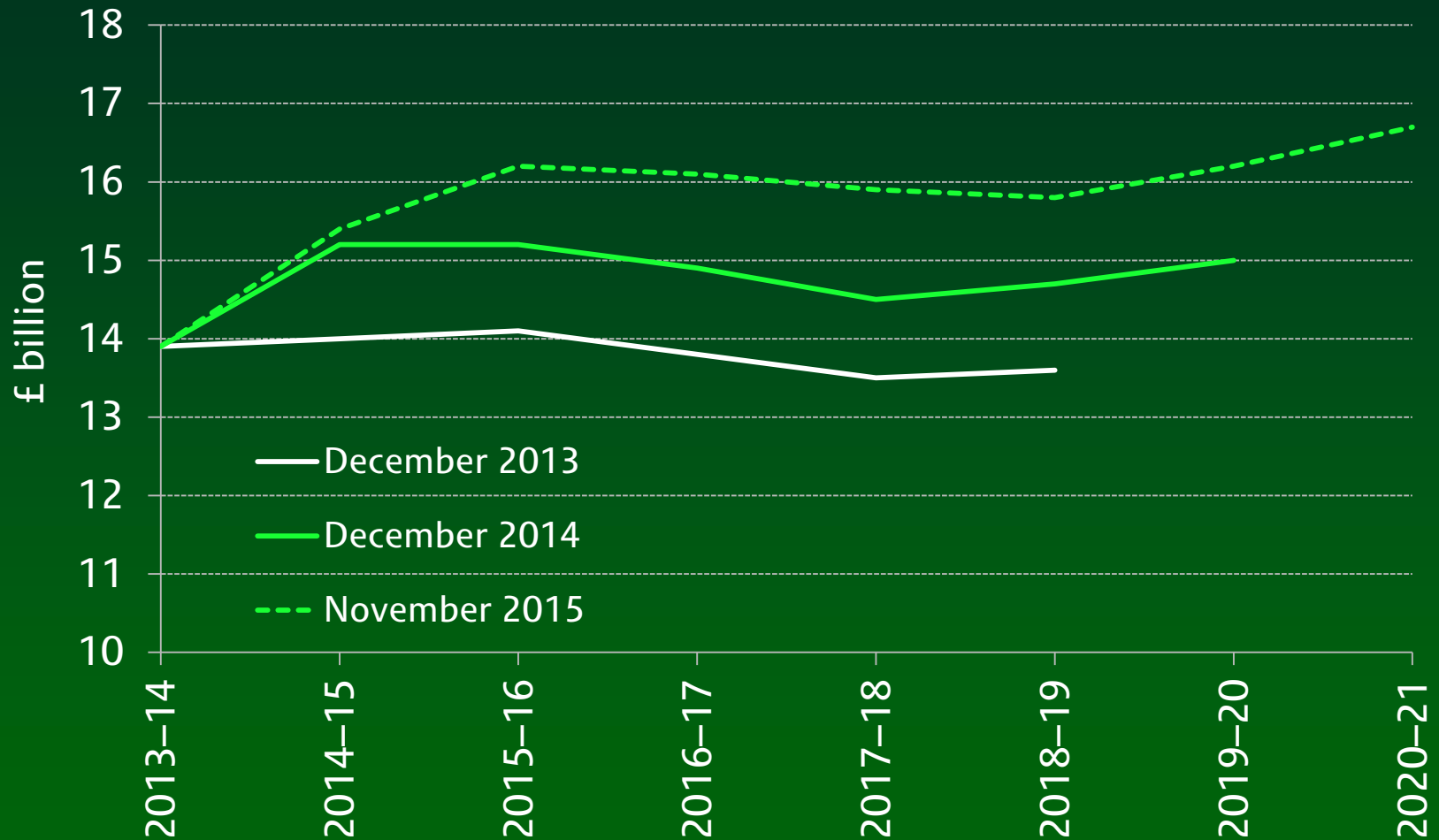
Risks to social security spending

- Social security spending to be reduced by £9 billion in real terms over next 5 years
 - £1 billion increase in spending on pensioner benefits
 - £10 billion decrease in spending on working age benefits
- Welfare cap in theory restricts upside risk on this area of spending
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 - further 4-year freeze in benefit rates will reduce levels significantly in real terms: has not been attempted in last 30 years
 - further delays in transition from Disability Living Allowance to Personal Independence Payments would increase spending

Revisions to expected costs of disability benefits



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 - delays to roll out of Universal Credit have ambiguous effect on spending: depends which aspect is delayed

Risks to debt interest spending

- Public spending sensitive to interest rates and inflation
- 1ppt increase (reduction) in gilt and short rates (from April 2016)
 - would increase (reduce) spending in 2019–20 by around £8 billion
- 1ppt increase (fall) in RPI inflation (from April 2016)
 - would increase (reduce) spending in 2019–20 by around £5 billion

Summary

- Good reasons to aim to reduce debt as a share of national income
- But commitment to deliver budget surpluses from 2019–20 risky
- Many risks to revenues, e.g.
 - recent equity price falls could depress capital tax receipts by £2 billion
 - manifesto commitments to cut income tax will cost £8 billion
 - continued inability to index fuel duty rates would cost £3 billion
- Many risks to spending, e.g.
 - further deep cuts planned to some areas of public services
 - population growth & ageing will put additional pressure on services
 - social security and debt interest spend could exceed current forecasts