

**25 JUNE 2009**

## **Welsh spending faces £2.2 billion cut between 2011 and 2014**

### **Eurfyl ap Gwilym assess the impact on Wales of the Chancellor's Budget statement**

An analysis of the UK 2009 Budget, presented to Parliament in April, shows that for the first time since the founding of the National Assembly in 1999, there will be *real* cuts in public expenditure in Wales.

Between 2011-12 and 2013-14 there could be a cumulative loss in *real* terms of £2.2 billion compared with the position if funding remained at the 2010-11 level for each of the following three years. Of this reduction £0.7 billion is in current expenditure and £1.5 billion in capital expenditure.

The UK Budget for 2009 was presented to Parliament on 22 April 2009 and has been the subject of much analysis and comment. What will be the likely impact of the Budget on devolved, identifiable public expenditure in Wales up to 2013-4.

The estimates made here are based on the Government's forecasts for the coming years as set out in the Budget 'Red Book' (HM Treasury HC 407) together with some analysis of the budget by the independent Institute for Fiscal Studies (IFS). It is not the purpose of this analysis to comment on the Treasury's budget forecasts but simply to use them as the basis for this analysis. It is clear that economic and financial forecasting for the coming years is very uncertain.

Wales received minimal attention both in the budget statement and in the related papers published by the UK Government. The one firm set of figures was for the Departmental Expenditure Limit for 2010-11 which showed that the Assembly Government's current expenditure would be £14.0 billion and capital expenditure £1.7 billion leading to a total devolved budget for Wales of £15.7 billion in 2010-11. This total compares with:

- An outturn of £13.8 billion in 2007-08.
- An estimated outturn of £14.6 billion in 2008-09.
- A planned £15.3 billion in 2009-10.

Thus the DEL for Wales will increase in nominal terms in the current 2009-10 financial year and also in 2010-11 (source: Table Col.11 of Budget Red Book 2009).

What will happen to the Wales devolved budget in the subsequent three years (2011-12 to 2013-14) will be covered in the Spending Review now expected to take place after the next UK General Election. Whilst the 2009 Budget does not spell out the forecasts for Wales there is sufficient information in the

Budget Red Book to come to an informed estimate based on two key statements by the Chancellor:

- UK current expenditure will grow at 0.7 cent per year in *real* terms from 2011-12 onwards.
- Public sector net investment will ‘move to’ 1.25 per cent of GDP by 2013-14. Moving to 1.25 per cent represents an average *real* cut of 17.2 per cent per year compared with current levels of 2.2 per cent of GDP.

Using this information allows an estimate to be made of the Departmental Expenditure Limit or the devolved budget for Wales up to 2013-14 and is set out in Table 1. *All estimates are in real terms, that is before allowing for inflation.*

**Table 1: Departmental Expenditure Limits (DEL): Wales (£billion)**

	<i>Plan</i> *		<i>Estimate</i> **		
	2009-10	2010-11	2011-12	2012-13	2013-14
Current	13.6	14.0	13.9	13.8	13.6
Capital	1.7	1.7	1.4	1.2	1.0
<b>Total DEL</b>	<b>15.3</b>	<b>15.7</b>	<b>15.3</b>	<b>15.0</b>	<b>14.6</b>
<b>Annual Change</b>	<b>-</b>	<b>+0.4</b>	<b>-0.4</b>	<b>-0.3</b>	<b>-0.4</b>

\* Table C 11. HM Treasury Budget 2009

\*\* Author’s estimate: see attached notes.

As can be seen from Table 1, for the first time since the establishment of the National Assembly in 1999, there will be *real* cuts in public expenditure in Wales. Between 2011-12 and 2013-14 there could be a cumulative loss in *real* terms of £2.2 billion compared with the position if funding remained at the 2010-11 level for each of the following three years. Of this reduction £0.7 billion is in current expenditure and £1.5 billion in capital expenditure.

These estimates are subject to a number of uncertainties:

- The Budget commentary is vague and unclear in many parts with respect to spending during the period covered by the next Spending Review and in particular regarding the treatment of efficiency savings and the resulting recycling of such savings.
- The economic forecasts on which the Treasury’s financial forecasts are based are uncertain and have been subject to considerable criticism by independent analysts and academics.
- It is assumed that cuts to the various departmental programmes will be evenly spread and, in the case of Wales, will be spread fairly evenly between devolved and non-devolved functions covered by departmental programmes (not Annual Managed Expenditure).

Notwithstanding these caveats, if the Welsh Assembly Government is properly to plan for the coming years it needs to make the best estimates possible of future funding levels whilst being mindful of the assumptions and underlying uncertainties. It is to be hoped that this is being done.

## Notes

The detailed assumptions made in arriving at these estimates are:

1. The Institute of Fiscal Studies has estimated that the 0.7 per cent annual *real* growth in total current expenditure during the next Spending Review period will be more than accounted for by growth in public expenditure on:
  - Servicing the increasing national debt.
  - Increased spending on social security.
  - Reflecting the growth in unemployment.
  - Other Annual Managed Expenditure.

Because of this the IFS estimates that total UK DEL expenditure will *reduce* by 2.3 per cent per year in real terms over the period of the next Spending Review up to 2013-14.

2. In the case of Wales changes to its Departmental Expenditure Limit are determined by applying the Barnett formula to *nominal* changes in the corresponding UK DELs. Assuming that RPI averages 2.0 per cent over the period in question then a *real* reduction of 2.3 per cent for total DEL equates to a *nominal* reduction of 0.3 per cent in the UK DEL and a *real* reduction of Wales DEL of 2.28 per cent and this is the figure used in this estimate. (When there are nominal increases in expenditure the Barnett formula gives rise to convergence but when there is a nominal cut there is Barnett divergence. In this case, given that RPI is almost equal to the real reduction in expenditure the difference is minimal).
3. There will, of course, be other reductions in public expenditure in Wales in the case of direct expenditure by UK government departments such as defence and non-devolved elements of, for example, transport.
4. This estimate also assumes that cuts in Departmental Expenditure Limits will be spread evenly across the various UK spending programmes. Given the materiality of expenditure on health and education at a UK level and their even greater materiality in determining changes to expenditure that is devolved (approximately 70 per cent of the total), it is difficult to see significant cuts in overall UK DEL not having an impact on these spending programmes and on the Wales DEL.
5. If the Government of the day decides to 'ring fence' expenditure on health, which appears to be Conservative policy, then other spending programmes will have to be cut more to make up the difference. If the greater cuts are made on those programmes that are not devolved then the cut to the Wales DEL could be less than projected here. Nevertheless it will not be possible to make the overall cut in DEL of 2.3 per cent without reductions in other

devolved functions such as economic development and transport. Spending on programmes that are controlled by UK Government departments and which have little or no direct spend in Wales such as the Cabinet Office and the Ministry of Justice are not material enough to absorb the total 2.3 a year reduction in UK DEL. In other words in any plausible scenario the Wales DEL will have to be cut.

6. In the case of capital expenditure the target reduction to 1.25 per cent of GDP by 2013-14 implies an annual real reduction of 17.2 per cent (such investment has been running at 2.2 per cent of GDP). For GDP the Treasury's forecast of GDP growth of 3.5 per cent per year from 2011-12 onwards has been used. If growth is lower then capital investment could be lower than indicated here. This estimate for the cut in capital expenditure agrees with the estimate arrived at independently by the IFS.

- **Eurfyl ap Gwilym is a Trustee of the IWA.**