

**Updated 22 May 2019**

## The Spending Review – background and prospects

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### Introduction

The Government is due to conduct a Spending Review in 2019. This will have major consequences for the jobs, pay and working conditions of everyone working in Government Departments, Agencies, NDPBs, and the wider public sector, as well as wider consequences for the UK's public services and economy.

The Chancellor had been aiming to conduct a full three-year spending review, which would set Departmental budgets up to and including the year 2023-24, by Autumn of this year. However continuing uncertainty over the Brexit process means it is now likely that this Autumn the Treasury will only publish plans for 2020-21.

Nevertheless this more limited exercise will have a major impact on public services in 2010-21, and is likely to be followed by a longer-term Spending Review – covering years up to 2023-24 and maybe beyond – next year, possibly as early as Spring.

This briefing sets out key background to the Spending Review and current expectations and questions about the direction it may take.

## Why it matters

Spending Reviews typically take place every three or four years, and set Departmental budgets (“resource” and “capital”) for future years. (In the past they have sometimes been called “Comprehensive Spending Reviews” or, if they cover only a single year, “Spending Rounds”). They are led by the Treasury and presented by the Chancellor to Parliament.

In theory it remains open to the Chancellor to adjust Departmental budgets year by year in the Annual Budget Statement. However this is relatively rare and marginal – for the most part Spending Review allocations are adhered to throughout the period covered, unless a General Election or change of Government results in a new Spending Review. For example, this financial year (2019-20) most departments are still working with Budgets that were set by George Osborne at the last Spending Review, in 2015.

The review taking place this year, and the one likely to follow it next year if it is initially restricted to a one-year horizon, will therefore be decisive in setting the context for the public sector into the middle of the next decade. Key questions that will be largely determined this or next year include:

- **recruitment, redundancies and staffing levels in 2020-21, 2021-22 and 2022-23.** The ability of Departments, Agencies, NDPBs and other public sector bodies to maintain (or grow) a workforce is largely a function of their “Resource” budget. The budget cuts entailed by the 2010, 2013 and 2015 Spending Reviews were the fundamental reason for the large number of redundancies and falling staff levels of the past decade.
- **pay for civil servants and other public sector workers in 2020-21, 2021-22 and 2022-23.** Sometimes Spending Reviews include an explicit pay policy – but even if they don’t, public sector employers’ ability to increase pay will be significantly constrained by the “resource” budgets they are working with (in 2019-20, though the Government has supposedly relaxed the 1% cap, most public sector employers still have to work with budgets that assumed it).
- **programme, administrative and capital budgets available to public sector employers in 2020-21, 2021-22 and 2022-23.** This will determine the ability of Departments, agencies, NDPBs and other public sector organisations to purchase equipment, provide training, invest in facilities, maintain support systems and many other things that will have a very direct impact on the working lives of their employees.

It is likely that civil servants and other public sector workers will be living with consequences of decisions that will be taken over the next six to eighteen months.

In turn, these consequences of the Spending Review allocations will be of critical importance to the quality and availability of the services that public sector organisations provide or the functions they carry out – and so to the strength of our economy, the state of our environment and the wellbeing of our society.

As the IFS says, the allocation of budgets for 2020-21 and beyond will constitute “one of the biggest non-Brexit decisions of the [current] parliament”.<sup>1</sup>

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<sup>1</sup> <https://www.ifs.org.uk/spring-statement-2019>

The following table shows the key decision points at which public sector budgets have, and will be, determined in recent and upcoming years.

<i>Fiscal year</i>	<i>Decision on departmental budgets</i>
2010-11	2007 Comprehensive Spending Review, led by Alistair Darling
2011-12	2010 Spending Review, led by George Osborne
2012-13	
2013-14	
2014-15	
2015-16	2013 "Spending Round", led by George Osborne
2016-17	2015 Spending Review, led by George Osborne
2017-18	
2018-19	
2019-20	
<i>2020-21</i>	<i>2019 Spending Review/Round, begun by Philip Hammond</i>
<i>2021-22</i>	<i>2020 Spending Review (probably); or (less likely) 2019 Spending Review</i>
<i>2022-23</i>	
<i>2023-24</i>	<i>2020 Spending Review (probably)</i>
<i>2024-25</i>	<i>2020 Spending Review (possibly, if a four-year review is decided on)</i>

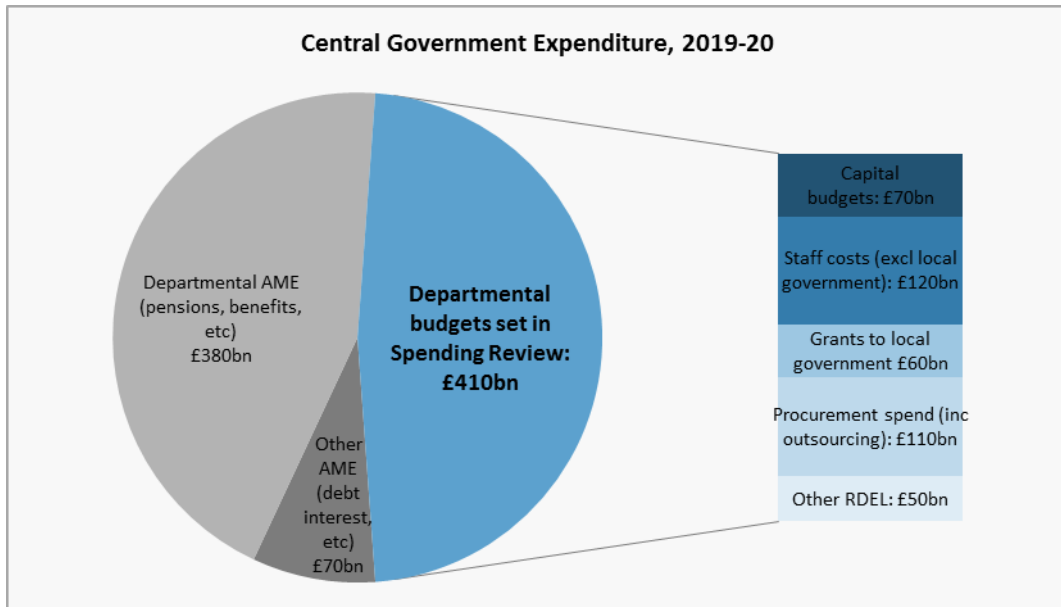
### **Background: Departmental budgets today**

Departmental budgets (or "expenditure limits") are split between "resource" spending (that is, day-to-day spending, more commonly described as "current") and "capital" (money for one-off investments in infrastructure or technology, for example).

(Another large area of government spending, known as "Annually Managed Expenditure" or AME, is not fixed in advance through Spending Reviews but managed year-to-year – this includes social security benefits and pensions, interest paid on government debt, and spending financed by tax raised at devolved or local levels).

Staff costs make up a large element of departments' resource spending, typically around half. Other items include expenditure on goods and services (such as materials and equipment, and outsourced services such as ICT or cleaning, catering or security).

A rough breakdown of total government spending in 2019-20 is set out below:

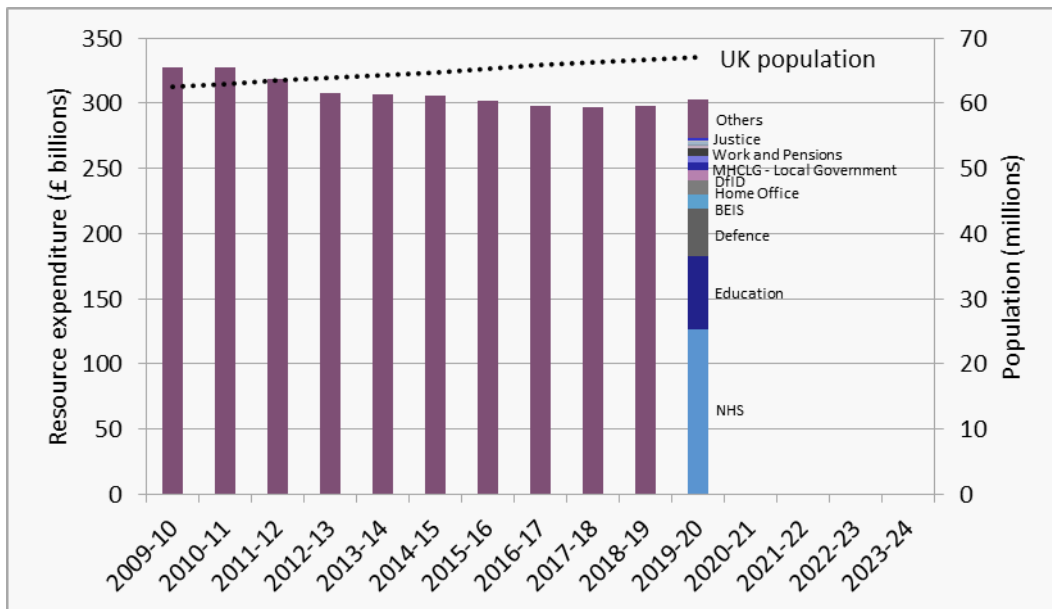


*Source: Public Expenditure Statistical Analyses*

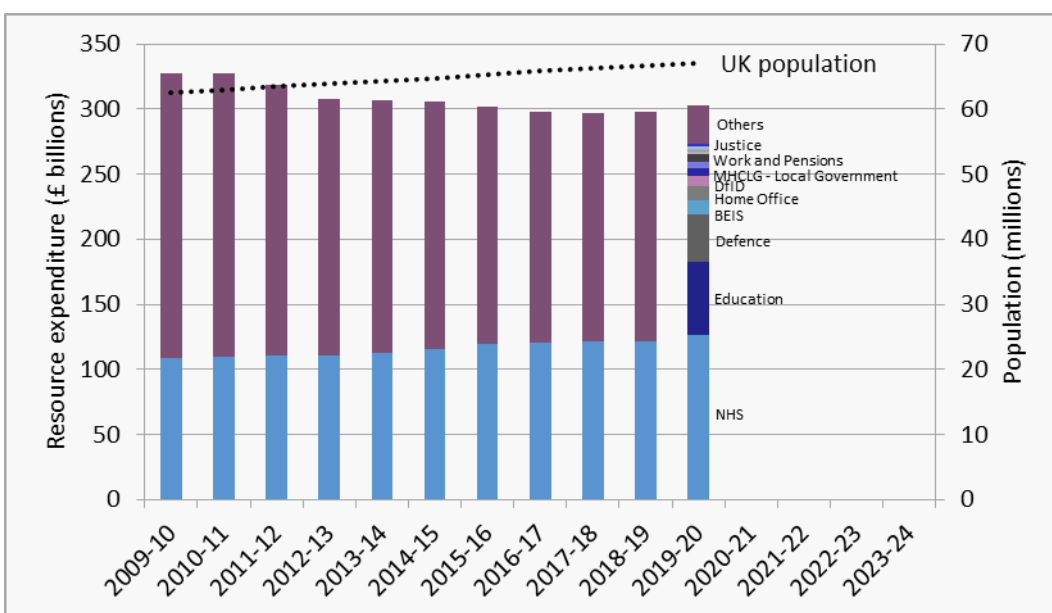
Departmental expenditure limits vary widely in size, the largest being the NHS, education and defence, and also in the balance between “resource” and “capital” components (BEIS and the Department for Transport are generally the most capital-intensive).



For almost every year of the past century, resource spending has risen in real terms in response to a growing population and other pressures such as rising expectations and costs. But over the past decade total resource spending has fallen in real terms, as a result of decisions taken in the 2010 Spending Review, the 2013 “Spending Round” and the 2015 Spending Review.

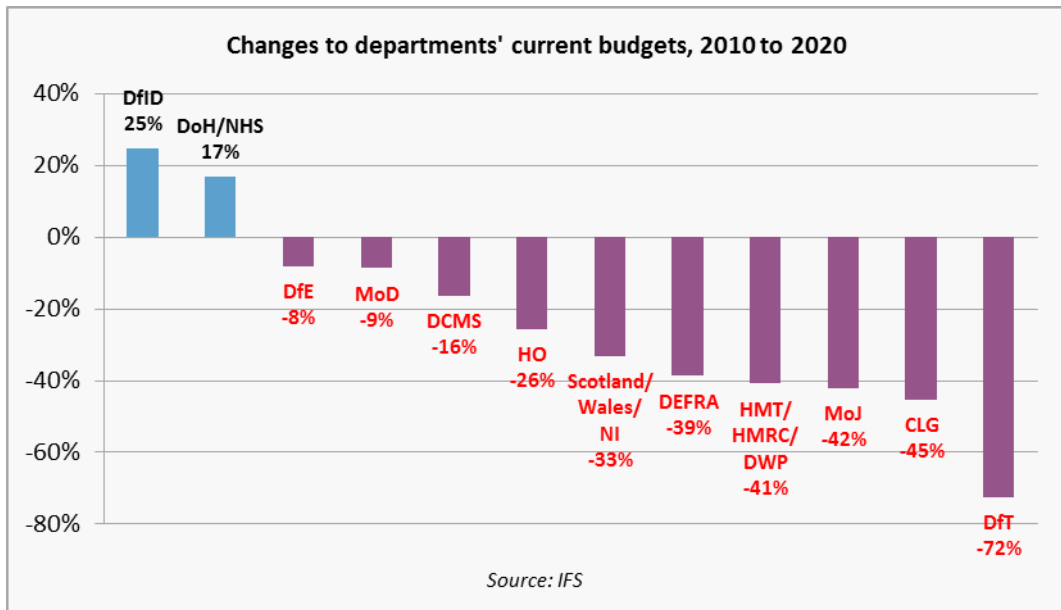


As the IFS notes, “It is unprecedented for departmental spending not to increase in real terms in a decade, and demands on departmental budgets will have increased significantly over that period”.<sup>2</sup> The impact of this tightening “envelope” has been even more severe than totals suggest because expenditure on the NHS has continued to rise in real terms (though more slowly than historical trends). This has further squeezed the amount of money available for other departments, agencies and NDPBs.



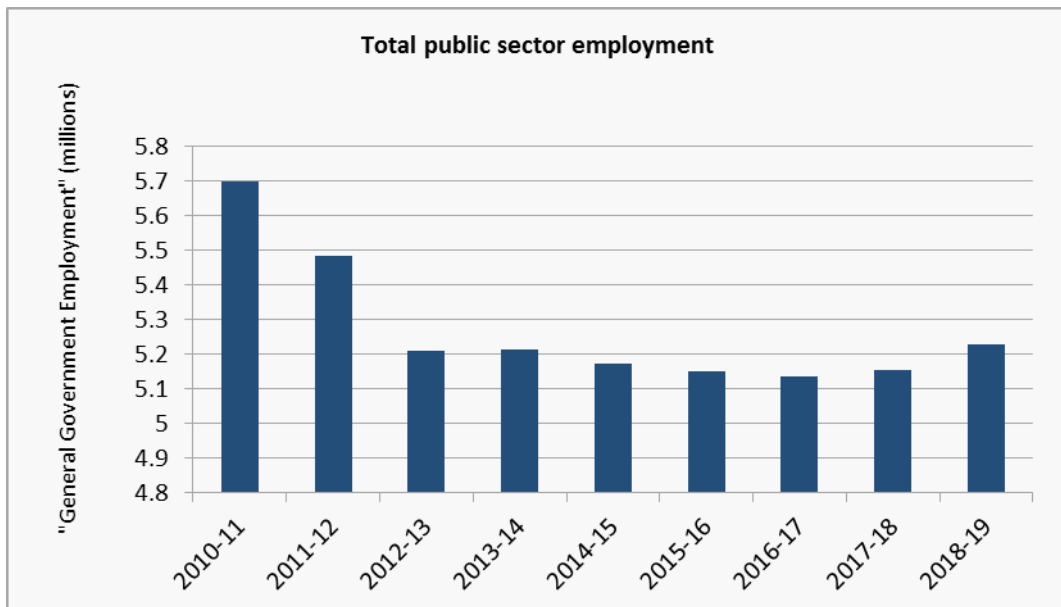
<sup>2</sup> <https://www.ifs.org.uk/uploads/publications/bns/BN243.pdf>

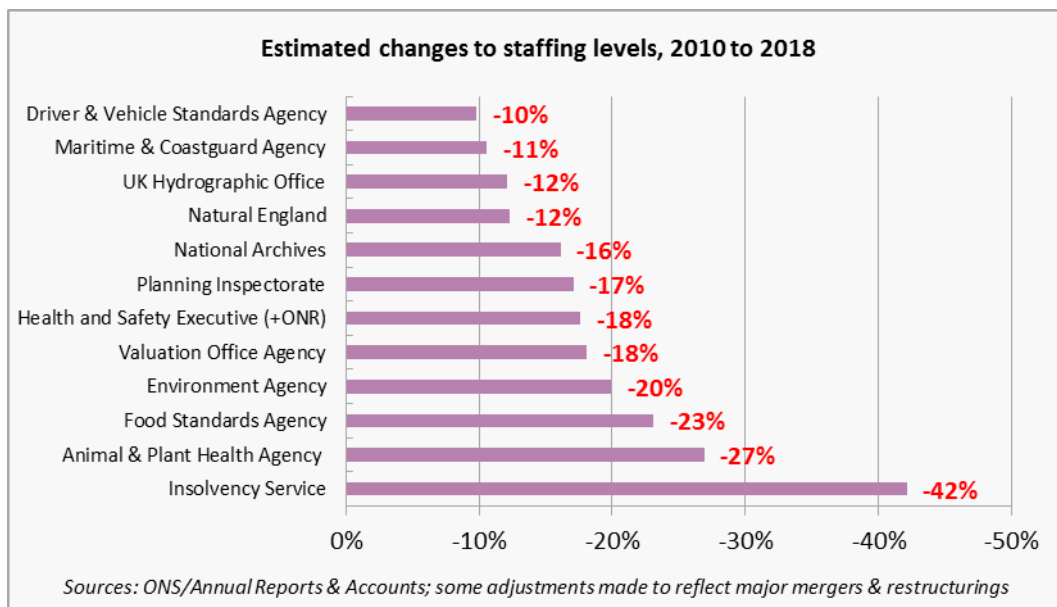
For some areas this has meant real terms cuts to resource budgets of 40% or more.



This has translated into sharp cuts in resourcing for many agencies and arms-length bodies, which rely wholly or largely on grants or other funding from parent Departments.

Total public sector employment has fallen by around half a million, or 10 per cent, since 2010, though it has increased slightly in recent years; in many areas the cuts have been even deeper than this and show no signs of being reversing.





Pay for civil servants and other public sector workers has fallen in real terms (against RPI) by more than 15 per cent as a result of pay policies announced in the 2010 and 2015 Spending Reviews. Although public sector pay policy was loosened to varying degrees in 2018-19, in all areas except the NHS this was not accompanied by any additional contribution to budgets which were set in 2015 on the assumption that pay would rise by no more than 1 per cent.

### **What we know about the next Spending Review**

The current political situation means that it is far from clear whether this year's Spending Review, and any that follows next year, will be completed by the current Chancellor, or even the current Government. Whoever is in charge of the process will however face the same parameters and options.

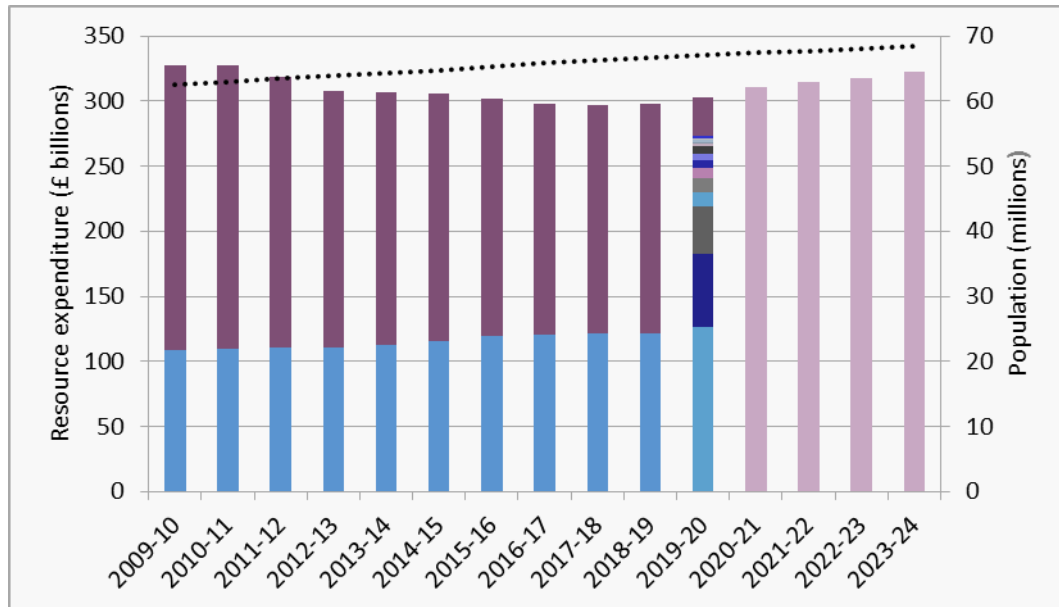
#### *The fiscal context*

UK economic growth is weak (around 1.5%) and currently forecast to remain so for the next five years. However, the public finances have been boosted by recent improvements in current and forecast tax revenues and falls in the rates of interest paid on Government debt. The current Chancellor's options have also been broadened by his decision to adopt a less rigid target for reducing government borrowing than his predecessor.

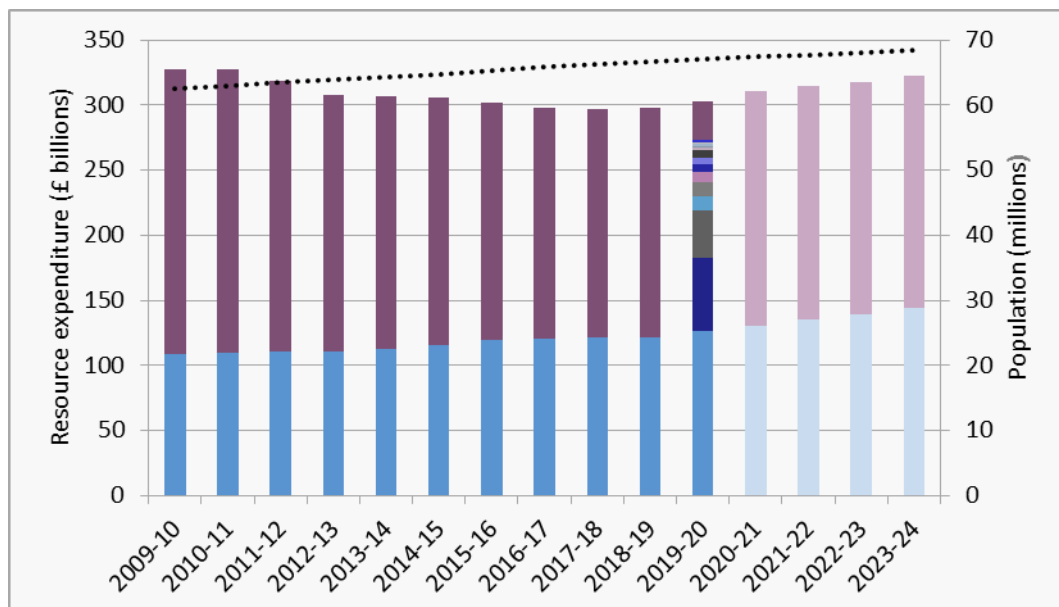
Against this background Philip Hammond has claimed that, subject to a "no deal" situation being averted, his fiscal position would allow him to commit increases in departmental spending that would amount to "an end to austerity". However he has also qualified this promise with the warning that on his definition this could still mean some departments continue to see their budgets cut in real terms.<sup>3</sup>

<sup>3</sup> "all Spending Reviews are about prioritisation and efficiency, and it would be odd to define ending austerity as meaning that every department sees an annual real terms increase in its budget"

There is not yet a final decision on what total spending on Departmental budgets will be for the years 2020-21, 2021-22, or 2022-23 (sometimes called the spending "envelope"). However the Treasury has published an "indicative path for public spending" which shows a change from the real terms reductions seen for much of the past decade, and the beginnings of a recovery relative to expected population growth.

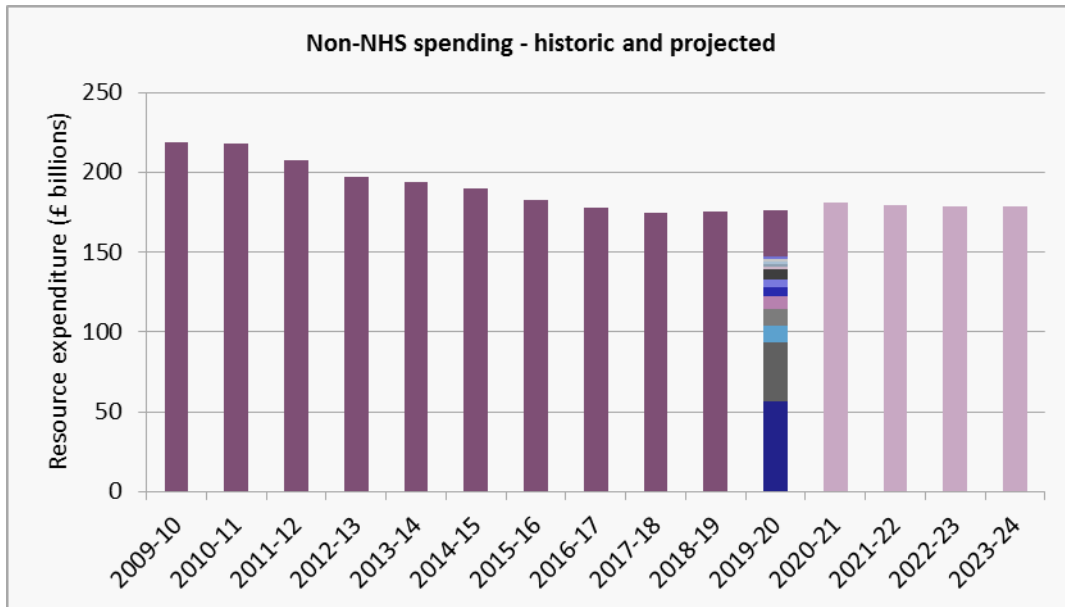


However the Government has already committed to an increase in spending on the NHS which effectively allocates a large portion of this projected spending total.





This would mean that, if the spending totals pencilled in by the Treasury become the fixed “envelope” for the Spending Review, the amount of spending left for departments outside the NHS would not see any significant real terms growth, as all the “new” money is taken up by the promised growth in NHS spending. This can be seen more clearly if the NHS budget is stripped out:

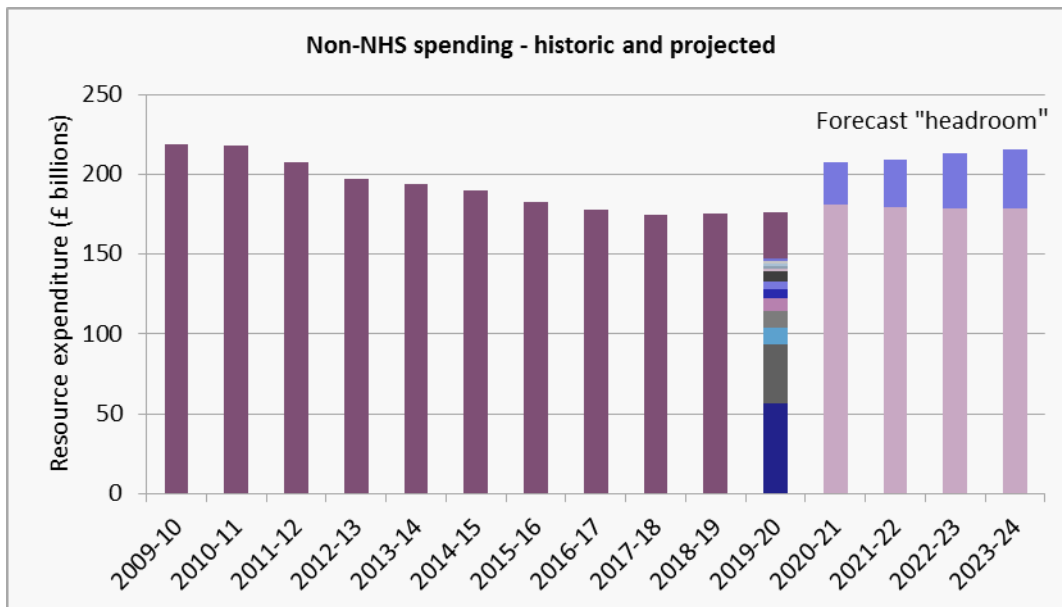


For this reason independent commentators have warned that, outside the NHS, the proclaimed “end of austerity” could prove disappointing. Especially if the Government wishes to continue to prioritise areas like schools and policing, and continue to adhere to international commitments to spend at least 2% of national income on defence and 0.7% on international aid, other areas could be looking at further years of significant real terms cuts.<sup>4</sup>

However any Chancellor could choose to increase total spending by more than currently projected, without even breaking the current targets for holding down government borrowing. Phillip Hammond has implied he is likely to do this if and when a Brexit withdrawal agreement is settled. (Until then, he has implied, he wishes to maintain “headroom” against his borrowing rule to allow for emergency spending to support businesses and the economy in the event of a disruptive “no deal” scenario).

According to the Resolution Foundation, this additional “headroom” that could be converted into extra spending would, on the latest official forecasts, rise to around £35bn in 2023-24, which could in theory allow the real terms cuts of the past ten years to be reversed.

<sup>4</sup> The IFS warned after the 2018 Autumn Budget: “this is no bonanza. Many public services are going to feel squeezed for some time to come. Cuts are not about to be reversed”.  
[https://www.ifs.org.uk/uploads/budgets/budget2018/pj\\_budget2018.pdf](https://www.ifs.org.uk/uploads/budgets/budget2018/pj_budget2018.pdf).



It is unlikely that the current Chancellor would in fact be minded to commit all this additional “headroom” on non-NHS departmental budgets. He might wish to allocate some of it to further cuts in borrowing; and/or additional capital spending; and/or tax cuts;<sup>5</sup> and/or increased spending on pensions or other social security benefits; and/or even further allocations to the NHS itself.

However even the limit set by the “headroom” is a political choice. A different Chancellor argue that current targets for borrowing and debt are too restrictive and that we should be ready to plan additional borrowing to fund public expenditure.<sup>6</sup> The scope for extra spending would also be increased if some taxes were increased, as a new Chancellor might be willing to do.<sup>7</sup>

### *Principles and priorities*

The most important influence on the Treasury’s allocation of budgets in the Spending Review is likely, as always, to be politics – from intra-Cabinet dynamics to wider public debate and opinion.

However there have been some indications of the principles and priorities the Treasury will seek to uphold, at least under its current leadership.

The **current Chancellor** stated in March 2019 that

<sup>5</sup> Potential Tory leadership contender Dominic Raab has proposed cutting the basic rate of income tax by 5p over five years, which would use up around £25bn of this headroom.  
<https://www.telegraph.co.uk/politics/2019/05/20/future-party-dominic-raab-liz-truss-matt-hancock-discuss-tory/>

<sup>6</sup> The IFS notes that “When governments are able to borrow at low interest rates – and in particular when long term interest rates are persistently lower than expected growth rates – the costs of high public debt are lower. In such an environment, the fact that debt is set to fall only slowly is perhaps less of a concern.”  
<https://www.ifs.org.uk/uploads/publications/bns/BN243.pdf>

<sup>7</sup> For example, abandoning plans to cut the main rate of corporation tax to 17% could raise around £6 billion a year. <https://www.gov.uk/government/statistics/direct-effects-of-illustrative-tax-changes>

“all Spending Reviews are about prioritisation and efficiency ... I intend to use the Spending Review to look at how we invest most effectively in our economy through a renewed focus on delivering high quality outcomes. The focus should be on what we achieve for public money, not just how much we spend.”<sup>8</sup>

Adopting a more explicitly political tone, the **current Chief Secretary to the Treasury** said in a recent speech:

“This year’s Spending Review ... allows us to make a real and lasting impact. We will have the power to modernise the state, making it sleeker, more effective and better value for the people it serves.”

The Chief Secretary promised a “People’s Spending Review”, stressing that “we should focus on people’s priorities not the blob of vested interests”. Her speech implied that this meant “money focussed on core public services – the police, education, roads, defence and the NHS”, not wasted on programmes advocated by the “growing blob of lobbyists, corporations, quangos and professional bodies who ask again and again for Government favours”. She also implicitly targeted “quangos”, “nanny state” programmes telling people “exactly how much to eat or how much to exercise”, and the kind of waste allegedly exemplified by EU spending on “donkey milk research projects”.<sup>9</sup>

**Treasury officials** have said they feel the need move Departments from a focus on “inputs” or budgets as such to have “more of an outcomes focus”.<sup>10</sup> A more detailed set of questions and criteria for budget allocations was set out alongside the Spring Statement, which stated that the Spending Review would “focus on public value outcomes”.<sup>11</sup>

This new “**Public Value Framework**”, informed by work commissioned from Sir Michael Barber, sets out key questions that public organisations should be asking themselves (or, by implication, can expect to be asked by the Treasury) to ensure they are making the best use of public money, grouped into four “pillars”:

1. “pursuing goals”, which “focuses on what overarching goals the public body is aiming to achieve and how it is monitoring the delivery of these”
2. “managing inputs”, which “tests the public body’s basic financial management”
3. “engaging citizens and users”, which “highlights the need to convince taxpayers of the value being delivered by spending and importance of engaging service users”
4. “developing system capacity”, which “emphasises the long-term sustainability of the system and the importance of stewardship”

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<sup>8</sup> <https://www.parliament.uk/documents/commons-committees/treasury/Correspondence/2017-19/Embargoed-Chancellor-to-Chair-Letter-re-Budget-report-response-280319.pdf>

<sup>9</sup> <https://www.gov.uk/government/speeches/what-should-the-spending-review-focus-on-speech-by-the-chief-secretary-to-the-treasury>. The speech was seen as playing to the Conservative base as candidates position themselves for a likely leadership race: <https://www.express.co.uk/news/politics/1102447/brexit-news-liz-truss-eu-deal-theresa-may-next-prime-minister-replacement>

<sup>10</sup> <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/spring-statement-2019/oral/98447.html>

<sup>11</sup>

[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/785618/WMS\\_final\\_Commons.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/785618/WMS_final_Commons.pdf)

Within the fourth pillar is a group of questions around “workforce capacity”. The document stresses the need for workforce planning processes based on “good, accurate workforce data” which can highlight issues such as “gaps in skills or professions. It also stresses the importance of attending to “changes required to the culture or behaviours” in an organisation to “support changes in delivery”. Key questions in this section include:

- “What processes and data does the public body use to monitor and plan for changes in its workforce?...”
- “Do these processes identify risks, such as skills or knowledge gaps and recruitment/retention issues?...”
- “How is the industrial relations context monitored and are contingency plans in place to respond to potential risks?...”
- “How does the public body intend to build the skilled workforce it will need to continue to deliver and adapt to future changes?...”
- “Does the strategy set out how the public body intends to attract and develop valuable key skills, such as commercial, finance, policy or transformation skills?”
- “Is the public body planning for the impact that new technology or automation could have on the workforce in future?”
- “Is there a strategy for embedding any necessary behavioural/cultural change that could be required in future?”<sup>12</sup>

It is not yet clear how exactly the “Public Value” framework will be applied to decisions on Departmental allocations in the Spending Review. Public sector leaders interviewed by Deloitte viewed it as “a powerful tool with profound implications – but were not convinced that it would be deployed with sufficient energy to fundamentally alter Spending Review 2019”.<sup>13</sup>

The Treasury has said that Departments will receive official guidance on submissions, which they will be expected to make before summer recess, and will then be assessed and discussed over a three-to-four month period.<sup>14</sup>

#### *Early expectations and speculation*

- Paul Johnson of the IFS has suggested it is possible the Government could go above its minimal commitment to meet the NATO target of spending 2 per cent of national income on **defence**<sup>15</sup> The current Foreign Secretary, in a speech widely regarded as

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<sup>12</sup>

[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/785553/public\\_value\\_framework\\_and\\_supplementary\\_guidance\\_web.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/785553/public_value_framework_and_supplementary_guidance_web.pdf)

<sup>13</sup> <https://www2.deloitte.com/uk/en/pages/public-sector/articles/spending-review-2019.html>

<sup>14</sup> <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/spring-statement-2019/oral/98447.html>;

<http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/spring-statement-2019/oral/99188.html>

<sup>15</sup> <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/spring-statement-2019/oral/99188.html>

seeking to position himself for a Tory leadership contest, has suggested the UK should “decisively increase the proportion of GDP we devote to defence”<sup>16</sup>

- It has been reported that “senior insiders” at UKRI are hopeful of generous increases in support for **research and development**: “it’s the first spending review in a while, where no one is preparing grim scenarios for budget reductions”<sup>17</sup>
- Officials interviewed by Deloitte have said that “the government retains its objective for greater regional equality and for **officials to relocate to regional hubs** as part of that agenda, and some expect relocations to form a substantial part of savings in the next Spending Review”<sup>18</sup>
- The Chief Secretary to the Treasury has told a local government audience that services and support for **SEND children** will be a particular priority<sup>19</sup>
- There is speculation that some politicians see the Spending Review as an opportunity to abandon **HS2**, and argue that funds could be reallocated to local transport projects<sup>20</sup>
- Tory leadership contender Dominic Raab MP has proposed closing down or merging **Government Departments** such as DIT and DfID to fund tax cuts. (In fact the 5p cut in income tax he proposed would cost around £25bn, more than the entire civil service paybill)<sup>21</sup>

This briefing will be updated as new information and analysis emerges. Please direct any queries or suggestions for inclusion to [martin.mcivor@prospect.org.uk](mailto:martin.mcivor@prospect.org.uk)

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<sup>16</sup> <https://www.bbc.co.uk/news/uk-politics-parliaments-48262331>

<sup>17</sup> <https://www.researchresearch.com/news/article/?articleId=1380810>

<sup>18</sup> <https://www2.deloitte.com/uk/en/pages/public-sector/articles/spending-review-2019.html>

<sup>19</sup> <https://www.lgcplus.com/politics/devolution-and-economic-growth/truss-spending-review-will-prioritise-send-children/7028898.article>

<sup>20</sup> <https://www.theguardian.com/uk-news/2019/apr/20/tories-conservatives-hs2-party-leadership-hopefuls-warned>

<sup>21</sup> <https://www.telegraph.co.uk/politics/2019/05/20/future-party-dominic-raab-liz-truss-matt-hancock-discuss-tory/>