Funding the Future

It's time for a stimulus - not cuts

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I was one of about 90 signatories to this letter issued last week. As with all these things, I don't agree with every word, but do with enough of the sentiment:

Open Letter to the Prime Minister and Chancellor

22 October 2021

A SPENDING REVIEW FOR A GREEN AND CARE-LED RECOVERY

Dear Prime Minister and Chancellor,

Your Budget and Spending Review next week give the Government the opportunity to demonstrate that its commitments to “building back better” and ”levelling up” after the pandemic are genuine and not just empty slogans. We urge you to use this opportunity to deliver the major increase in public investment needed to rebuild the economy on a secure and sustainable footing.

In particular we urge you not to let the misguided economics implied by the rhetoric of “fixing the public finances” determine your choices. Consolidating the public finances before the recovery is well on its way would be highly economically and fiscally irresponsible.

The UK’s economic recovery from Covid is already slowing down under the impact of supply chain and labour shortages. The latest figures show unemployment at more than one and a half million people, or 4.5% of the labour force.[1] Around a million people were estimated to be still on the furlough scheme when it ended on September 30th, and employment is not expected to recover to pre-Covid levels for years to come.[2]

At the same time your government has made welcome commitments to tackling the climate and environmental crisis, reducing geographic inequalities, and building a proper social care system.

In the US, President Biden has shown how ambitious public investment, supported by borrowing and taxation, can drive broad-based prosperity and job creation.[3] The UK has one of the lowest rates of overall investment in the developed world.[4] And at just 2.2% of GDP, public investment is also considerably lower than the OECD average of 3.3%.[5]

As in the US, the UK still has room for public borrowing. The pandemic has raised public debt to around 100% of GDP, but what really matters is how much the government is spending to service the debt, and the value of the spending which the borrowing finances. In fact near-zero interest rates mean that the government's debt service payments are now at their second-lowest level since 1950, at just 6% of tax receipts.[6] Moreover the Bank of England owns nearly 40% of the debt, and repays any profit on the interest it receives back to the Treasury.[7] It can continue to support borrowing at low interest rates.

Public investment will repay its financing over time through higher taxes and revenues as fiscal and wider economic multipliers kick in. We know from the experience of austerity that attempting to cut debt by cutting public spending is self-defeating and does not work.[8]

It would therefore be a grave economic error to focus now on "fixing the public finances" by cutting back vital investment and public spending. As we saw during the austerity years, the human cost of doing so would be felt most acutely by those at the sharp end of inequality.

We urge you therefore to use the Budget and Spending Review to introduce a fiscal stimulus package of around £70-90bn in annual spending over the next three years over and above current plans, equating to 3-4% of GDP. This would be the level which would return the UK economy to its pre-pandemic growth path and stabilise public debt. We believe the stimulus should be focused on a green and care-led recovery, with a major focus on investment in disadvantaged areas. This would meet the Government's own stated goals and would enable you to start building the critical infrastructure - both physical and social - needed for a thriving modern economy.

In particular:

* Around £30bn a year in green investment would put the UK on track to meet its legal net zero emissions target and its commitment to nature restoration. It would create over half a million jobs, spread throughout the country.[9]

* Social care needs much higher investment. With the government's announced increase in National Insurance contributions earmarked for the NHS not social care, at least £11 billion in additional funding is needed to deliver free personal care for the over-65s, secure a pay rise to the Real Living Wage for social care workers, and improve access to care in people's own homes. To build an adult social care system in which all those eligible get care free at the point of use, both for adults aged 18-64 and

those over 65, would require £29bn a year.[10]

* Around £10bn a year over and above current spending should go to childcare, enabling parents of young children, especially women, to participate fully in the labour market, and thereby to earn incomes and spend them in the economy.[11]

Of the total stimulus package we propose, about half would be in capital spending, and half current. Such a package, including fair pay increases for public sector workers and a restoration of local government funding, would boost and sustain the economic recovery. It would raise demand and private sector investment, improve productivity and, through the fiscal and wider economic multipliers, pay for itself through higher tax receipts.

The green and social infrastructure spending we propose would be spread across the country, with particularly beneficial economic effects in disadvantaged areas where unemployment is highest and incomes lowest.

To ensure that "levelling up" is real and not just rhetorical, the Treasury should publish a comprehensive Equality Impact Assessment of its spending and budget plans, and should mandate the Office for Budget Responsibility to conduct a subsequent evaluation. This should include the proportion of spending going to the poorest third of local authorities measured by the Index of Multiple Deprivation, and the impact of its measures on women, black and minority ethnic groups, people with disabilities and others.

Higher tax receipts over recent months have given the Chancellor some headroom for higher spending. The bulk of the investment we propose should be funded by borrowing. But there is also a very strong case for making the tax system fairer. As a minimum we would urge you, like your predecessor Nigel Lawson, to bring the tax rates on income from wealth (including capital gains and dividends) in line with those on income from work.[12] There is also a clear opportunity to levy a windfall tax on excessive profits made during the pandemic, particularly by digital companies.[13] Announcing a longer term review of how land and property wealth can be more fairly taxed would also serve the country and the economy well.[14]

We welcome the Government's commitments to build back better from the pandemic, to level up the economy, to achieve net zero, and to reform social care. In this Budget and Spending Review you can demonstrate that you take these commitments seriously and intend to deliver them. We hope that you will do so.

Yours sincerely,

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Notes

* ***https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/bulletins/employmentintheuk/latest***

* ***https://www.resolutionfoundation.org/publications/job-well-done/***

* ***https://www.investopedia.com/joe-biden-s-economic-plan-save-the-middle-class-4769869***

* ***https://tcdata360.worldbank.org/indicators/inv.all.pct?country=GBR&indicator=345&countries=BRA&viz=line_chart&years=1980,2024***

* ***https://www.statista.com/statistics/650030/public-sector-net-investment-as-share-of-gdp-united-kingdom/; https://www.oecd-ilibrary.org/sites/1c258f55-en/1/3/2/14/index.html?itemId=/content/publication/1c258f55-en&_csp_=10e9de108c3f715b68f26e07d4821567&itemIGO=oecd&itemContentType=book***

* ***https://docs.google.com/document/d/1CccmBzyFhrIBYGkBsxP487hkEIdJuo5eZL16jk94UcA/edit***

* ***Michell, J (2021), forthcoming; https://www.omfif.org/2020/12/raising-bank-of-england-rates-risks/***

* ***https://www.primeeconomics.org/s/The-Economic-Consequences-of-Mr-Osborne-2016-final-v2-8.pdf***

* ***For the calculations underlying this figure, see the Briefing Note accompanying this letter***

* ***Ditto***

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* ***https://www.tuc.org.uk/news/tuc-raising-tax-wealth-could-give-61000-social-care-workers-london-pay-rise; https://www.ippr.org/research/publications/just-tax***

* ***https://www.ippr.org/research/publications/prosperity-and-justice-after-the-pandemic; https://www.taxjustice.uk/blog/six-companies-made-16-billion-in-excess-profit***

s-during-the-pandemic

* **https://www.ippr.org/research/publications/the-invisible-land**