Human City **HEADLINES**

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Public Debt, the Comprehensive Spending Review & the Potential Effects on 'Human' Cities

SUMMARY

- The UK's National Debt began in the late 17th Century and remained at least 25 percent of Gross Domestic Product (GDP) throughout the next three hundred years. During the 18th Century it grew to 260 percent of GDP; more than three times the current deficit. It then took the next 100 years to reduce the National Debt and for 60 of those years it was above the current level. The National Debt then exploded in World War I, continued to grow during most of the 1920s and 1930s and then increased steeply during World War II.

- In 1945 the National Debt stood at 216 percent of GDP. It took the next twenty years to reduce the National Debt to the level the UK has currently. In fact, the National Debt remained above 100 percent of GDP between 1920 and 1960.

- The UK's National Debt is relatively low historically and in comparison to competitor economies. Previous National Debt reductions were undertaken relatively slowly. 'Zero' has not been achieved since the 1690s. This throws into relief the plan to dramatically reduce the deficit over the life of a single Parliament. Previous reductions were achieved through a growing economy, reductions in unemployment and boosting tax revenues, as well as freezing or reducing public expenditure marginally.

- The UK has considerable advantages in the structure of its deficit. Around £7 in every £10 of the deficit is held within the UK unlike many other comparable countries where external investors are the holders, and financed over a longer term.

- The objectives of reducing public expenditure as rapidly and by such an extent (more than £80 billion) as outlined in the Comprehensive Spending Review can be questioned against this historic backdrop. The projected loss of 490,000 public sector jobs amid already growing jobs loss and insecurity, variable business confidence, housing market slowdown, ballooning council waiting lists, and the spectre of the dreaded double-dip, is risky and may have severe effects on the 'humanity' of the UK's cities.

- The effects of the CSR will be broadly regressive; those most likely to be affected are people on welfare benefits, the low paid, poor families, the young, those dependent upon services delivered by local authorities and social housing tenants. HCI's conclusion is that the effects of the CSR will likely widen inequalities between the top and the bottom of the income scales. And that community cohesion in the UK's city might be adversely affects.

Introduction

Reducing the public sector deficit has provoked debate about a number of interrelated issues. Firstly, is the size of the public sector deficit unprecedented in UK economic history as many claim? Secondly, what are the causes of the current deficit; typically, what is due to excessive expenditure on the public realm (the so-called structural deficit) and what to the worldwide banking crisis? Thirdly, is the UK's deficit unusual among comparable countries? Fourthly, what are the alternative ways of reducing the deficit and over what timescales? Lastly, since the Coalition Government has included a 'fairness' test within the Comprehensive Review, what will be the potential effects of austerity economics upon the 'human' characteristics of the UK's cities and citizens following the Comprehensive Spending Review?

This bulletin from the Human City Institute (HCI) seeks to illuminate the first four of these questions by examining historic data. It then moves on to provide a summary of potential effects of austerity economics on the policy areas which HCI researches; mainly economic sustainability, social justice and equality, community cohesion, housing and neighbourhoods, public health and generally the 'power of place' to produce discernible effects on life chances. All of the charts in the bulletin are based on 2010 data from HM Treasury, the Office of National Statistics (ONS) and the International Monetary Fund (IMF). Unemployment projections are based on a HCI extrapolation of ONS data for the 2011 to 2015 period.

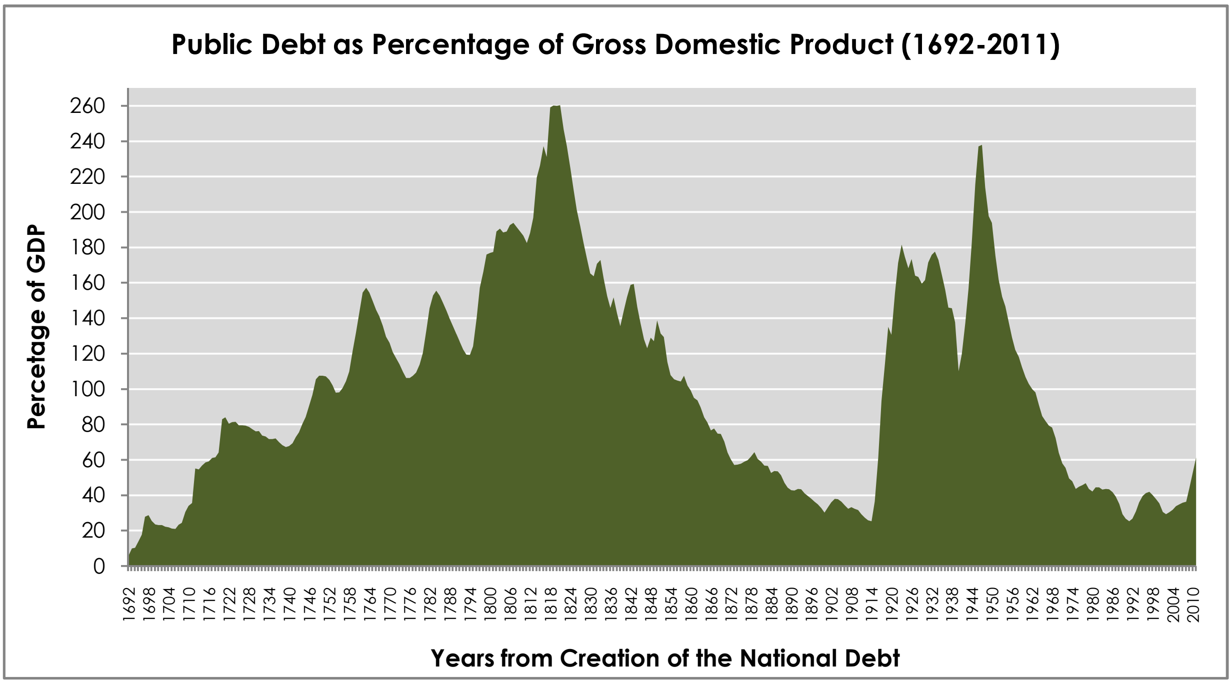
How Does the UK's Public Sector Deficit Compare?

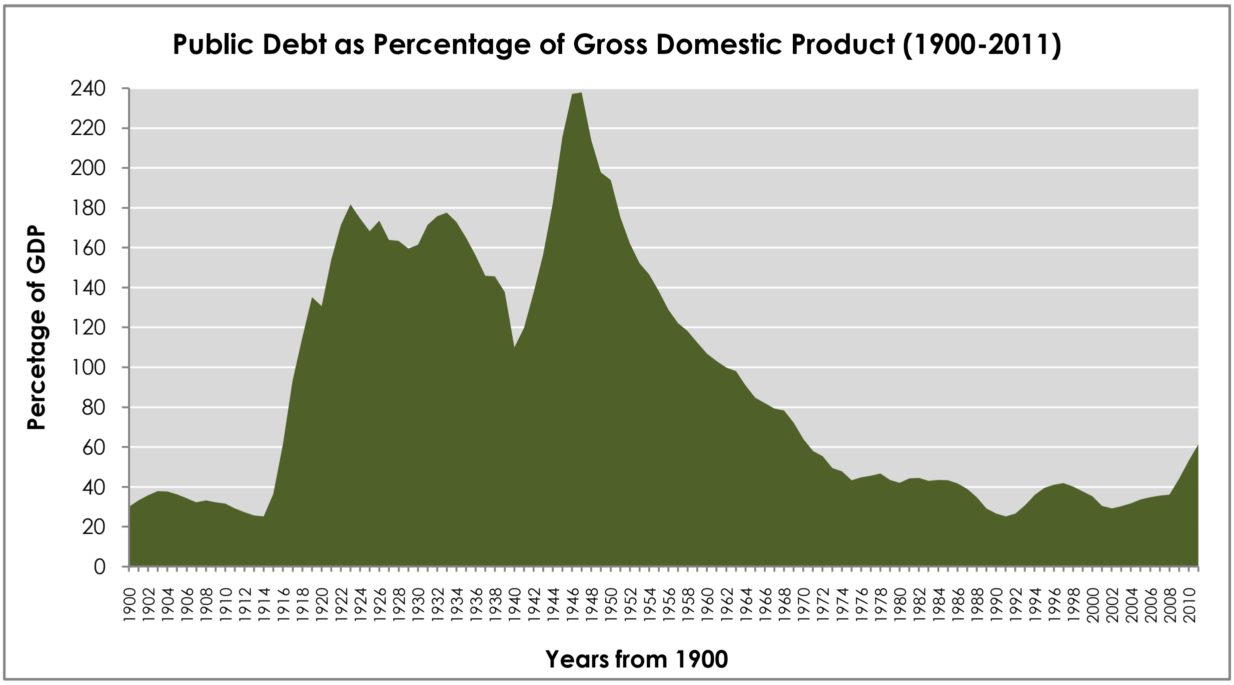
Reviewing the historic origins of the UK's public sector deficit (cumulatively called the National Debt) are important since they enable assessment of how unusual the current deficit is and to compare what the National Debt looked like at previous times of national economic emergency, economic expansion or during wars. The two charts over the page provide an overview of the National Debt as a percentage of Gross Domestic Product (GDP - the value of all economic activity in monetary terms) by year. The first provides a 300 year and the second a view since 1900 so that peaks and troughs are more easily discernible.

The beginnings of the UK's National Debt can be traced back to William III who in 1692 engaged a syndicate of City merchants, which later became the Bank of England, to market an issue of, in today's terminology, Government bonds. Throughout the 18th Century, the National Debt grew to finance the Duke of Marlborough's wars, wars against the French and the North American colonial rebels, and into the 19th Century, the Napoleonic Wars. The National Debt during this approximate 120 years grew to 260 percent of GDP; more than three times the current deficit (at just over 70 percent). It then took the next 100 years to reduce the National Debt and for 60 of those years it was above the current level.

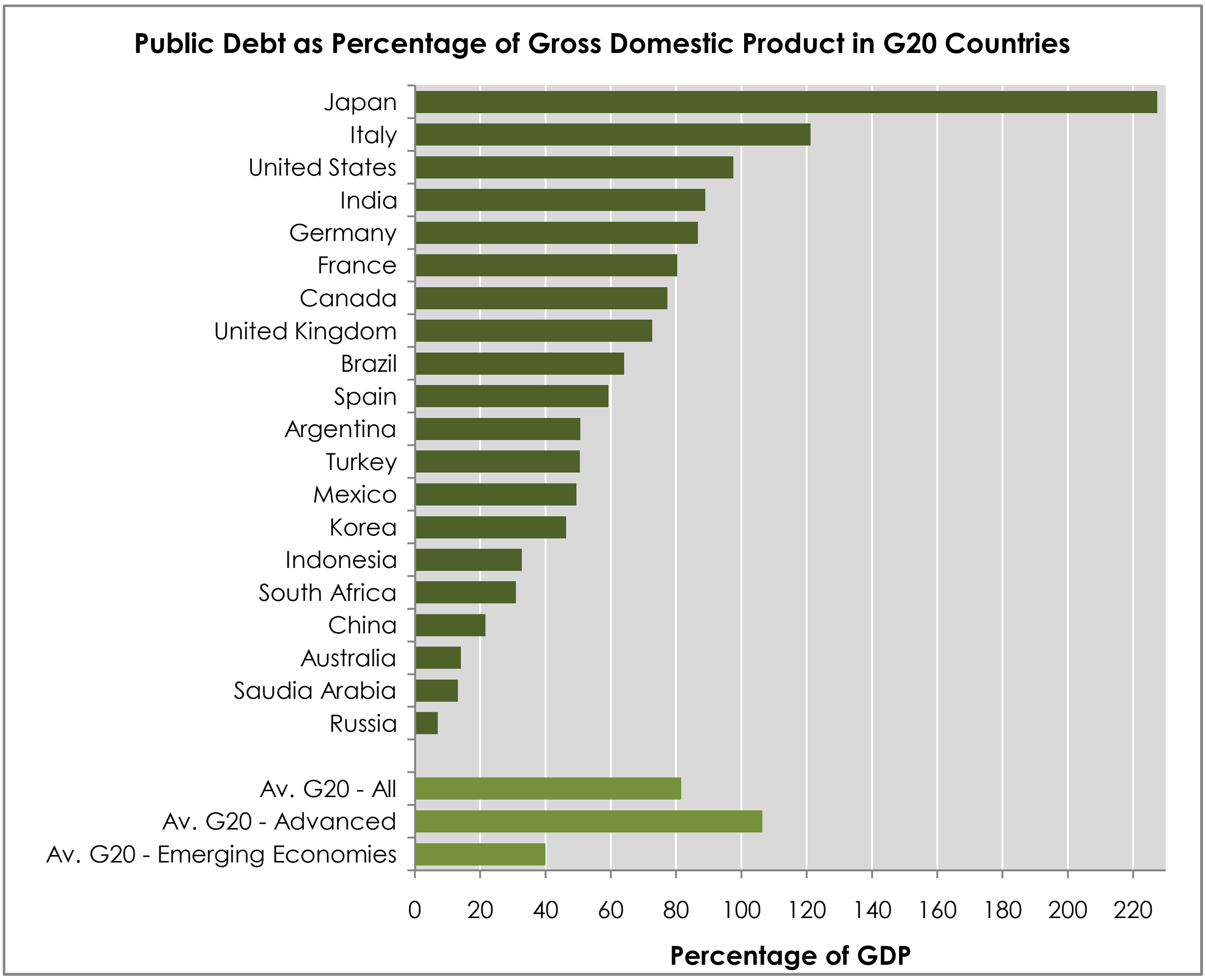
The National Debt then exploded in World War I, continued to grow during most of the 1920s and 1930s, as the Great Depression dawned, and then increased steeply during World War II. In 1945 the National Debt stood at 216 percent of GDP. It took the next twenty years, until England won the World Cup in 1966, to reduce the National Debt to the level the UK has currently. In fact, the National Debt did not fall below 100 percent of GDP, a proportion that many commentators now claim is unmanageable, even once between 1920 and 1960.

The National Debt averaged 40 percent for the period of Conservative Government between 1979 and 1997, when the National Debt stood at 42 percent. When New Labour came to power, the National Debt was reduced in successive years until it reached a low of 29 percent in 2002. It then began to rise, reaching 36 percent in 2008, but still very low compared to the long-term and in contrast to most of the 1980s and 1990s.





The increased emphasis upon public expenditure by the New Labour Government was the main driver behind the growth in debt over the 2002 to 2008 period. However, when the international financial crisis hit in 2008, the National Debt more than doubled over the next two years. The chief causes of this rapid ballooning were the bailing out of UK banks, the shrinking of the UK's economy by 6 percent, an increase in unemployment and a collapse in tax revenues. The international nature of the crisis can be shown by comparing the debt to GDP ratios of similar countries (see the following chart for G20 members). The UK has the lowest ratio in the G7 (lower than Japan, Italy, USA, Germany, France and Canada). The UK has an average ratio when compared across the whole G20 and is significantly below average when only 'advanced' G20 members are included.



The preceding points to a number of conclusions:

- The UK's public sector debt is relatively low when using historical precedents and in comparison to competitor economies. An historical overview also shows that previous National Debt reductions were undertaken relatively slowly and generally over decades. 'Zero' has not been achieved since the 1690s, and as with most advanced countries, probably never will, since borrowing is often associated with economic dynamism (reference the USA and Japan with far larger economies than the UK and India with a much faster growth rate).

- Reductions have usually been achieved through a growing economy, reductions in unemployment and boosting tax revenues, as well as freezing or reducing public expenditure, as the Labour and Conservative Governments did in the late 1970s and early 1990s, and as the Conservatives did in the early 1990s. This throws into relief the plan to dramatically reduce the deficit over the life of a single Parliament.

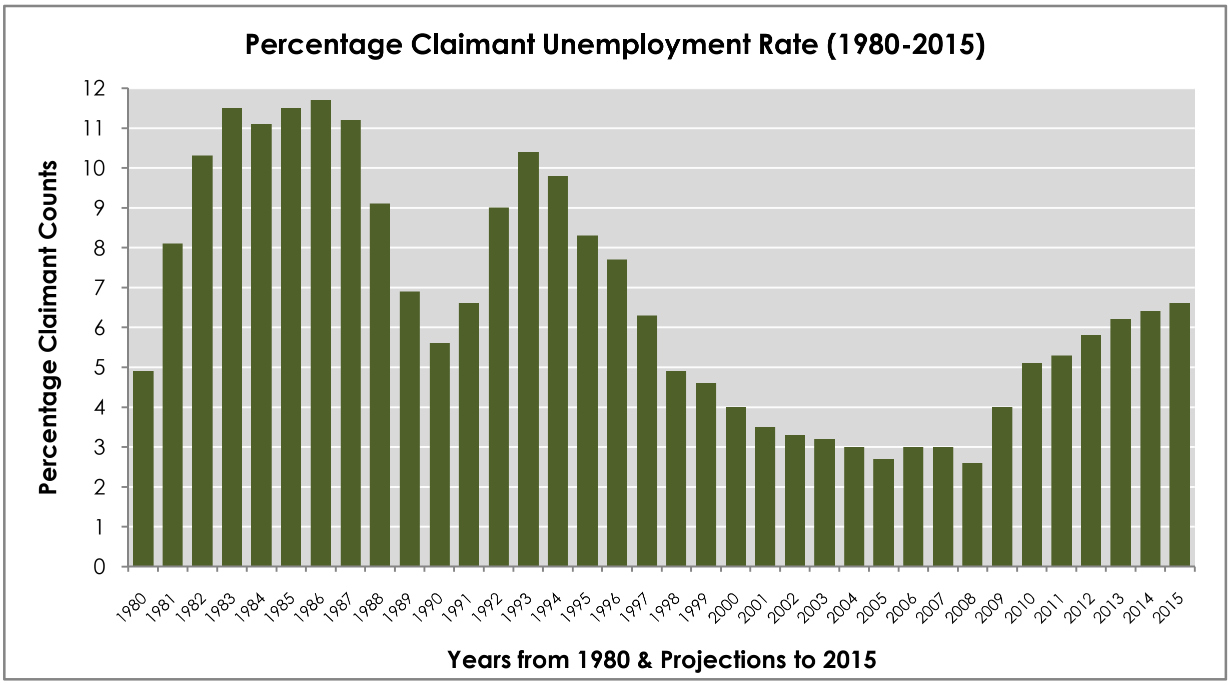
- The UK has considerable advantages in the structure of its deficit. Around £7 in every £10 of the deficit is held within the UK unlike many other comparable countries where external investors are the holders. Additionally, the UK's deficit is financed over a longer term of more than 12 years compared to typically 7 years for competitors, meaning that refinancing is less frequent and subject to speculative pressures, and is so more sustainable.

Potential Effects of the Comprehensive Spending Review

The objectives of reducing public expenditure as rapidly and by such an extent (more than £80 billion) as outlined in the Chancellor's statement to the House of Commons on 20th October can be questioned against the historic analysis previously outlined. The projected loss of 490,000 public sector jobs amid already growing jobs loss and insecurity, variable business confidence, housing market slowdown, ballooning council waiting lists, and the spectre of the dreaded double-dip, is risky and may have the following effects.

- **Economic Sustainability:** The Chancellor has achieved some sustained investment in transport infrastructure (most notably refurbishment of Birmingham's New and the Mersea Gateway bridge) and some other capital projects. The Green Investment Bank also got the go-ahead. On wider economic issues, HCI calculates that for every £1 saved from reductions in the public sector job losses only £0.50p is actually saved because of loss of taxes and benefits take-up. The reduction in public spending is equivalent to around 7 percent of GDP, a hole which will need to be filled by private sector growth, which seem unlikely given the state of the international economy.

- **Social Justice, Equality & Fairness:** Increases in the International Development budget are welcome since they move the UK closer to agreed 'End Poverty' targets. The protection of the health budget, and to a lesser extent education spending, which received a boost from the pupil premium, will protect some of the most vulnerable and support children from disadvantaged backgrounds. Reductions in welfare benefits, on top of those already announced in the aftermath of the General Election, coupled with changes to the tax and tax credit systems, point to all sections of society bearing some of the deficit reduction burden. However, consensus opinion, including that outlined in the Coalition Government's own Comprehensive Spending Review document points to those most severely affected being people on welfare benefits, the low paid, poor families, the young, those dependent upon services delivered by local authorities and social housing tenants. HCI's conclusion is that the effects of the CSR will be broadly regressive and likely to widen socio-economic inequalities between the top and the bottom of the income scales.



- **Unemployment & Community Cohesion:** The cohesion of communities in the UK's cities, as revealed by the unrest experienced in the 1980s in Handsworth, Toxteth and St Paul's, is closely linked to unemployment levels. HCI expects unemployment to rise conservatively to around 7 percent in 2015 from less than 3 percent at the start of the international financial crisis in 2008, but only if the private sector can create compensatory employment and economic growth does not stall following the retrenchment of state funding. If the economic falters, however, unemployment is likely to rise close to 1980s levels with concentrations in already vulnerable communities and fragile local economies. Reductions in public services by local authorities and police numbers, likely to lead to less community policing, may impact on the most disadvantaged communities.

- **Housing & Neighbourhoods:** Social housing has been affected particularly severely with around 60 percent of the capital budget for new house building disappearing over the next five years. New tenants will have their security of tenure curtailed and will need to pay up to 80 percent of market rents to access the social housing sector. Although the Coalition Government expects social landlords to be able to build up to 150,000 new homes through increased rental streams, it seems probable that social housing will become even more 'residualised' than at present, and a declining proportion of the national housing stock at a time when housing waiting lists are growing (1.8 million households at present) and the home ownership market remains unaffordable to most newly forming households.

- **Public Health & the 'Power of Place':** While the NHS budget is protected and will see a small real increase in funding over the next five years, the changed management of primary care - consortia of GPs to replace Primary Care Trusts - leaves a question mark over the delivery of public health, which affects inequalities in health between rich and poor, Black and White, young and old, renters and home owners. HCI's research shows that the 'power of place' is crucial in determining inequalities in health in a city setting - life expectancy varies by as much as 12 years between the inner city and more affluent suburbs. Consequently, disinvestment in spend on social housing, regeneration programmes, Sure Start and the uncertain future of public health are all likely to contribute to growth in health inequalities.

The analyses above and the views expressed in the bulletin are those of the author.

Kevin Gulliver
Director - Human City Institute
21st October 2010

About the Human City Institute

HCI is an independent, charitable 'thinktank' undertaking research into 'human city' issues, investigating exclusion and promoting solutions to the problems of the most disadvantaged groups in today's complex and diverse cities, towns and communities.