

Wales Fiscal Analysis briefing note

Counting consequentials

Analysing the Welsh Government Final Budget 2019-20 and Local Government Settlement

On 18 December 2018, the Welsh Government published its Final Budget for 2019-20. This briefing looks at the changes from the Draft Budget in October, the implications for Welsh Government departmental spending and local authorities, and briefly assesses the outlook for future Welsh budgets beyond 2019-20.

Implications of the UK Autumn Budget

Shortly after the publication of the Welsh Government Draft Budget for 2019-20, the UK government published its own budget on 29 October. As ever, there was confusion and contradictions in claims of the extra funding made available to the Welsh Government.

Headlines suggested spending decisions taken by the UK government had resulted in [an extra £554 million for the Welsh Government](#) to spend over three years. However, around £365 million of this figure related to consequentials from the NHS funding announcement from July, which had already formed a part of the Welsh Government's spending plans outlined a week previously. There were even claims that some of that extra money had [not in fact materialised](#).

The Welsh Government's Final Budget documents finally provides some clarity over the implications of the Autumn Budget.

The block grant for day-to-day spending in 2019-20 has increased by around £100 million since the publication of the Welsh Draft Budget in October. This increase reflects two main factors:

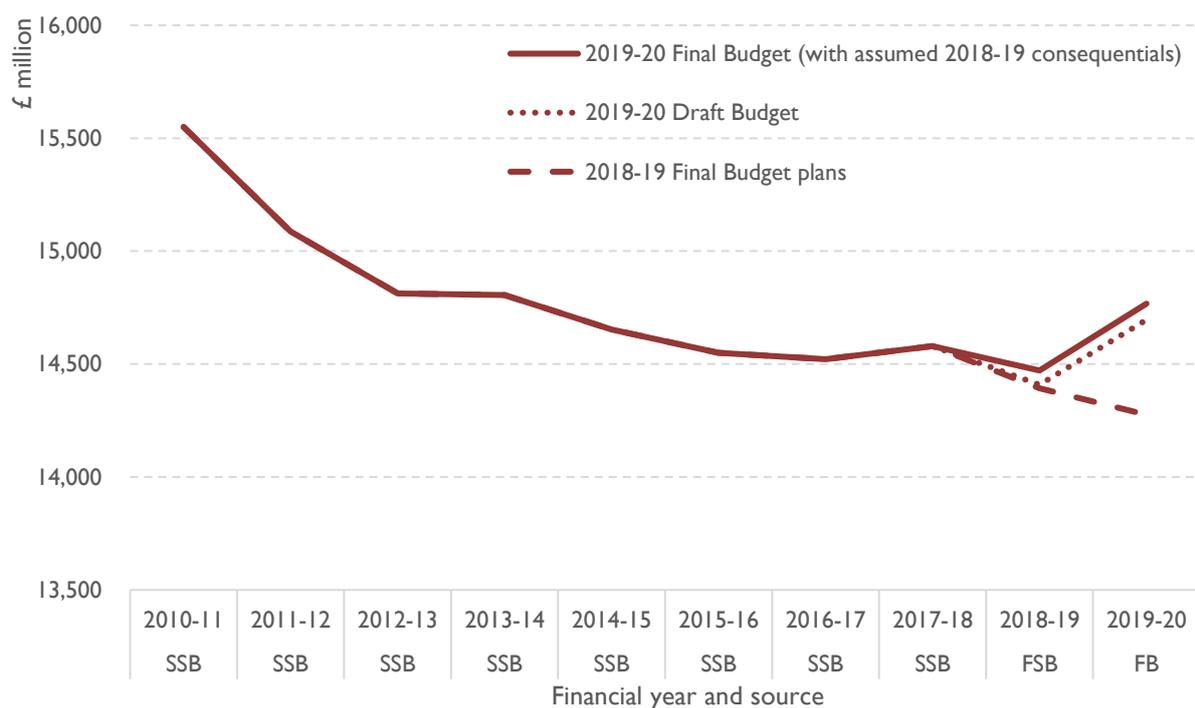
- £40 million is a reduction to the Block Grant Adjustment (the BGA – or the amount taken off the block grant to account for income tax devolution in 2019-20). The increase to the personal allowance announced by the UK government at the Autumn Budget has lowered the forecast for devolved income taxes, and as 2019-20 is the first year of devolution, the BGA has been adjusted to ensure the Welsh Government does not lose out.

- Approximately **£60 million results from extra consequentials in the Autumn Budget.**¹

The Welsh Government has also decided to allocate a further £12.1 million to departments from what was previously unallocated fiscal resource.

This means that the **amount allocated to departments for day-to-day spending on public services has increased by around £72.9 million** since the Draft Budget publication in October. As shown in figure 1, this represents a significant increase from the spending plans for 2019-20 laid out at this time last year. The allocated fiscal resource DEL is over £500 million higher than originally planned, a result of extra consequentials and an increased draw-down from the Welsh Reserve.

Figure 1: Trend in fiscal resource DEL (including Non-Domestic Rates), 2010-11 to 2019-20 (2018-19)



Welsh Government day-to-day spending will increase by over 2% in real terms in 2019-20, by far the largest increase since before the start of austerity measures in 2010-11. It will still be around 5% lower in real terms than in 2010-11 however.

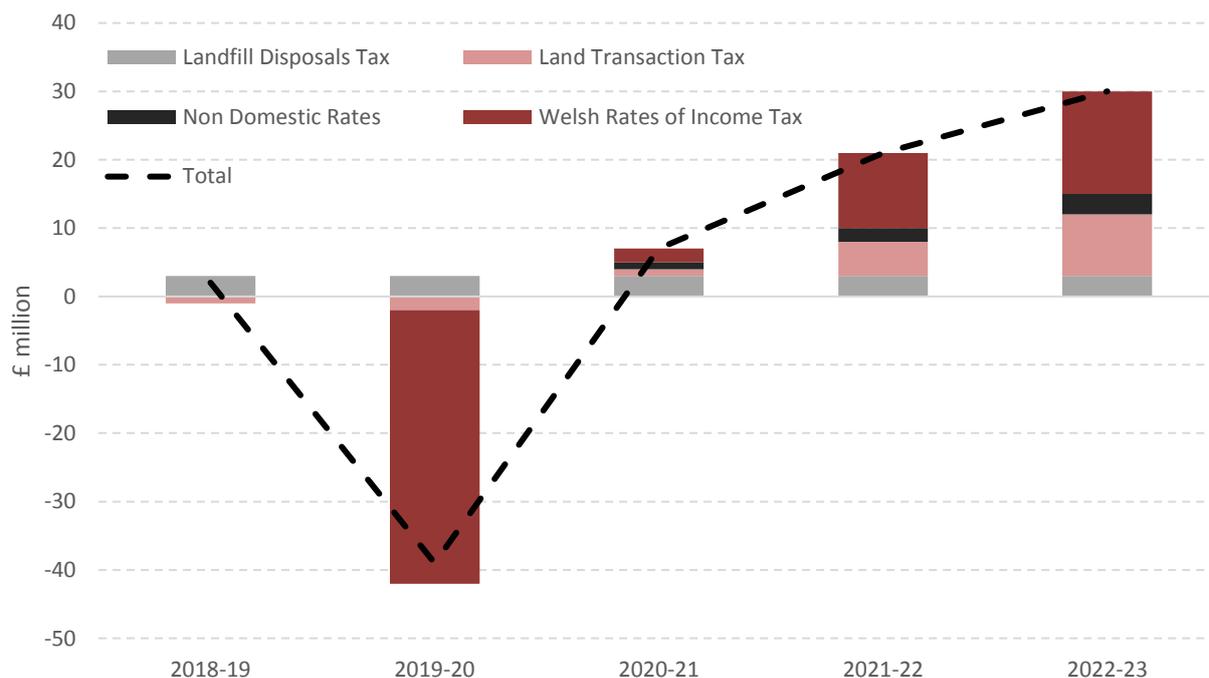
On the capital side of the budget, the majority of consequentials for capital spending from the Autumn Budget was for the current financial year (2018-19), though the capital block grant for 2019-20 has increased by around £10.6 million. The Welsh Government has also allocated a further £27.5 million from its unallocated capital finance, the majority of which will go to local authorities' general capital fund.

¹ A small portion of this may be attributable to a revision in the forecasts for the two smaller devolved taxes and the corresponding block grant adjustments, but figures on block grant adjustments are yet to be published.

Changes to devolved tax forecasts

While there are no changes in tax policy in the Final Budget, there were some revisions to devolved taxes forecasts since October (shown in figure 2). As explained above, the biggest revision is a £40 million downward revision to devolved income tax revenue, which will not have a budgetary impact for the Welsh Government. In later years of the forecast however, income tax revenues have been revised upwards slightly. Similarly, there is a slight downward revision in Land Transaction Tax revenue in the first years of the forecast, reflecting both changes to the underlying economic forecasts and updates to the forecasting methodology.

Figure 2: Revisions to the forecast for devolved taxes revenue from October to December



By the final year of the forecasts (2022-23), total revenue has been revised up by £30 million. However, since these forecasts are influenced by UK level data and trends, this is likely to be broadly matched by increases in the BGA (determined by revenue trends in England and Northern Ireland).

Departmental allocations

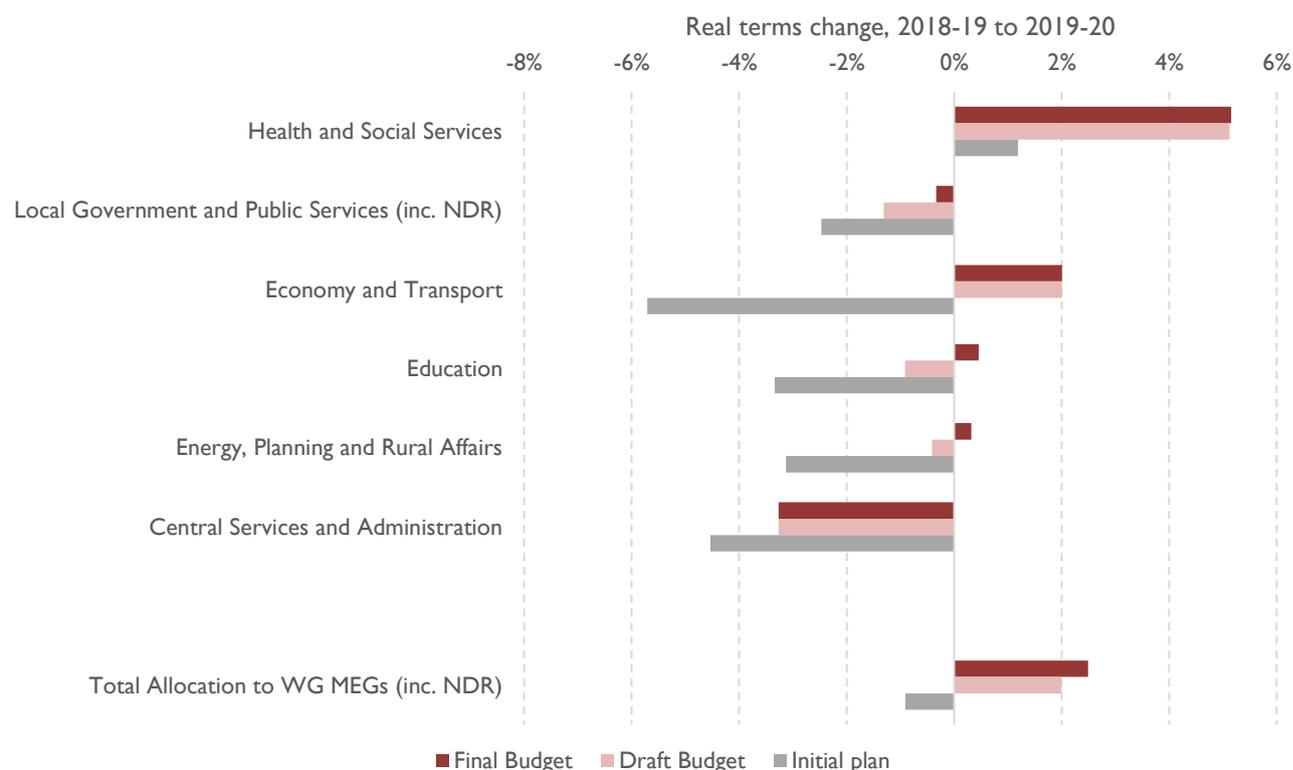
The Welsh Government had stated that local government would be [“front of the queue”](#) for extra funding resulting from the Autumn Budget. On 20 November, the then Cabinet Secretary for Finance Mark Drakeford laid out [proposals for additional funding](#) for local authorities.

Figure 3 compares the planned change in spending from 2018-19 to 2019-20 by Welsh Government department (Main Expenditure Groups – or MEGs), according to initial plans laid out last year (grey bars), the draft budget plans (light red bars) and the updated final budget plans (dark red bars).² While

² These year-on-year changes compare plans for 2019-20 with spending for 2018-19 outlined in the First Supplementary Budget for 2018-19. This doesn't take into account any extra allocations to departments for

Health and Social Services saw the biggest increase from original plans, the Local Government and Public Services MEG has been the biggest beneficiary of decisions taken this December.

Figure 3: Real terms change in total fiscal resource DEL allocations to departments (MEGs) from 2018-19 to 2019-20



The allocation to the Local Government and Public Services MEG increases by over £47 million compared to the Draft Budget. Of this total, the Welsh Government has fully passed on the consequential received as a result of business rates relief in England to enhance the Welsh Government’s high street rates relief scheme by £23.6 million.

As announced on 22 November, the revenue support grant (RSG) to local authorities was increased by £13 million, providing a cash-flat settlement (see later section), with an additional £1.2 million in top-up funding to ensure no local authority faces a reduction of more than 0.5% (up from a 1% floor set in October). The revised settlement also includes £2.4 million for local authorities to provide discretionary NDR relief and a further £7 million to increase the capital limit to £50,000 for those having to pay for social care.

There are also a number of specific grants in other MEGs which will affect local authority spending. A further £7.5 million has been allocated in the Education MEG to fund the teacher’s pay award (on top of the £13.7 million announced in the Draft Budget), and £2.3 million for children’s social services in the Health and Social Care MEG.

Other significant spending changes announced in the Final Budget include £4.8 million for pay deals in Further Education colleges and £6.8 million towards delivering all-age apprenticeships (both in the Education MEG).

2018-19 which will be made at the Second Supplementary Budget in February 2019, including any consequentials from the Autumn Budget for 2018-19 (expected to be around £63 million).

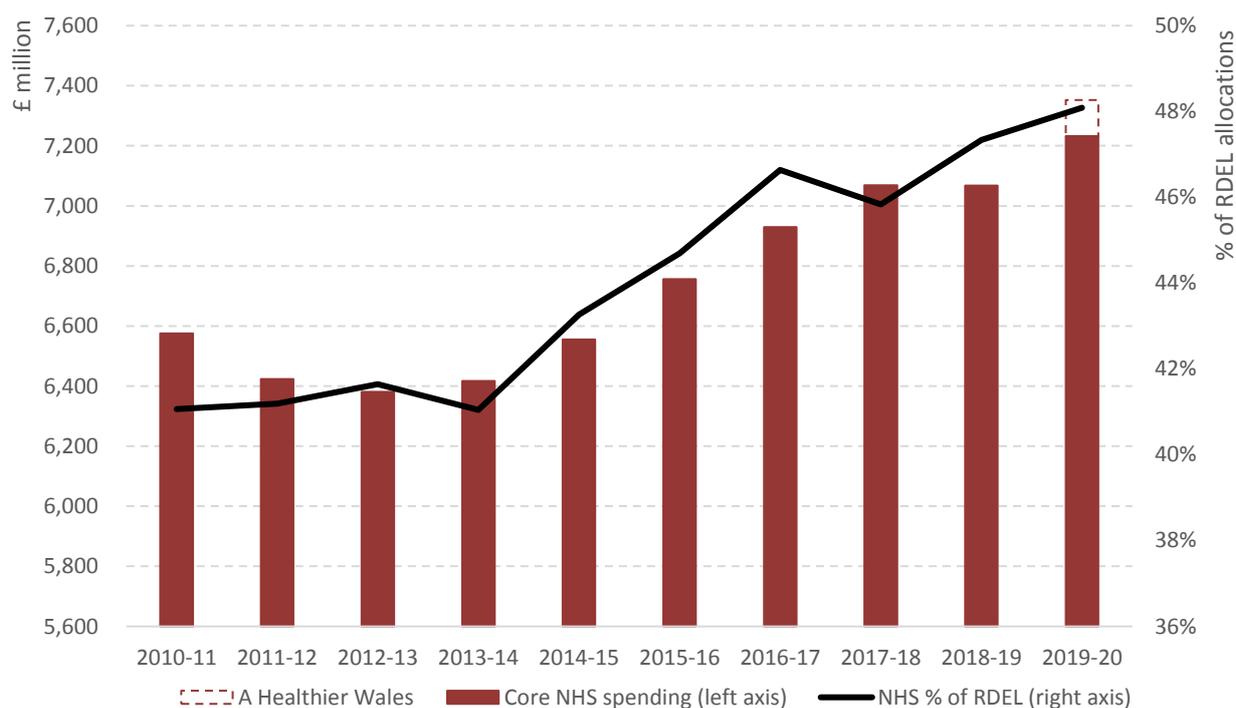
Health

The extra resource already allocated to health spending in October meant there was no further change announced in the Final Budget.

The presentation of NHS spending in the budget this year looks different compared to previous years, partly a reflection of the increased interlinking with social care spending, and changes to education and training budget lines (which has been moved into the central Health Education Improvement Wales budget). To build a consistent time series, we aggregate across budget expenditure lines (subtracting some elements) to get a measure of core NHS spending.³ Including the estimated health element of the 'A Healthier Wales' budget line, we estimate day-to-day health spending will increase by 4% in real terms to 2019-20.⁴

Figure 4 presents core NHS spending from 2010-11 to 2019-20, and as a share of Welsh Government departmental day-to-day spending. After falling in real terms over the first years of austerity, NHS spending has increased by an average of around 2.3% a year in real terms since 2013-14. In 2019-20, we estimate NHS spending will account for around 48% of day-to-day spending, up from 41% in 2013-14.

Figure 4: Allocations to core NHS spending and as share of day-to-day spending, 2010-11 to 2019-20 (2018-19 prices)⁵



³ Included in the 2019-20 figure is funding for the delivery of core NHS services, targeted NHS services, education and training spending, mental health spending and the substance misuse action plan fund, but Public Health Wales spending is excluded. This roughly corresponds to what would have been called NHS Delivery and Health Central Budgets in previous budget documents.

⁴ This year there is a new budget line worth £192 million for the implementation of *A Healthier Wales*, a plan to create an integrated health and social care system. We include in this analysis an estimate of the 'health' component of this spending line (excluding some spending such as a special grant for local authorities to address social care pressures).

⁵ 2018-19 and 2019-20 figures may change according to allocations made at future supplementary budgets.

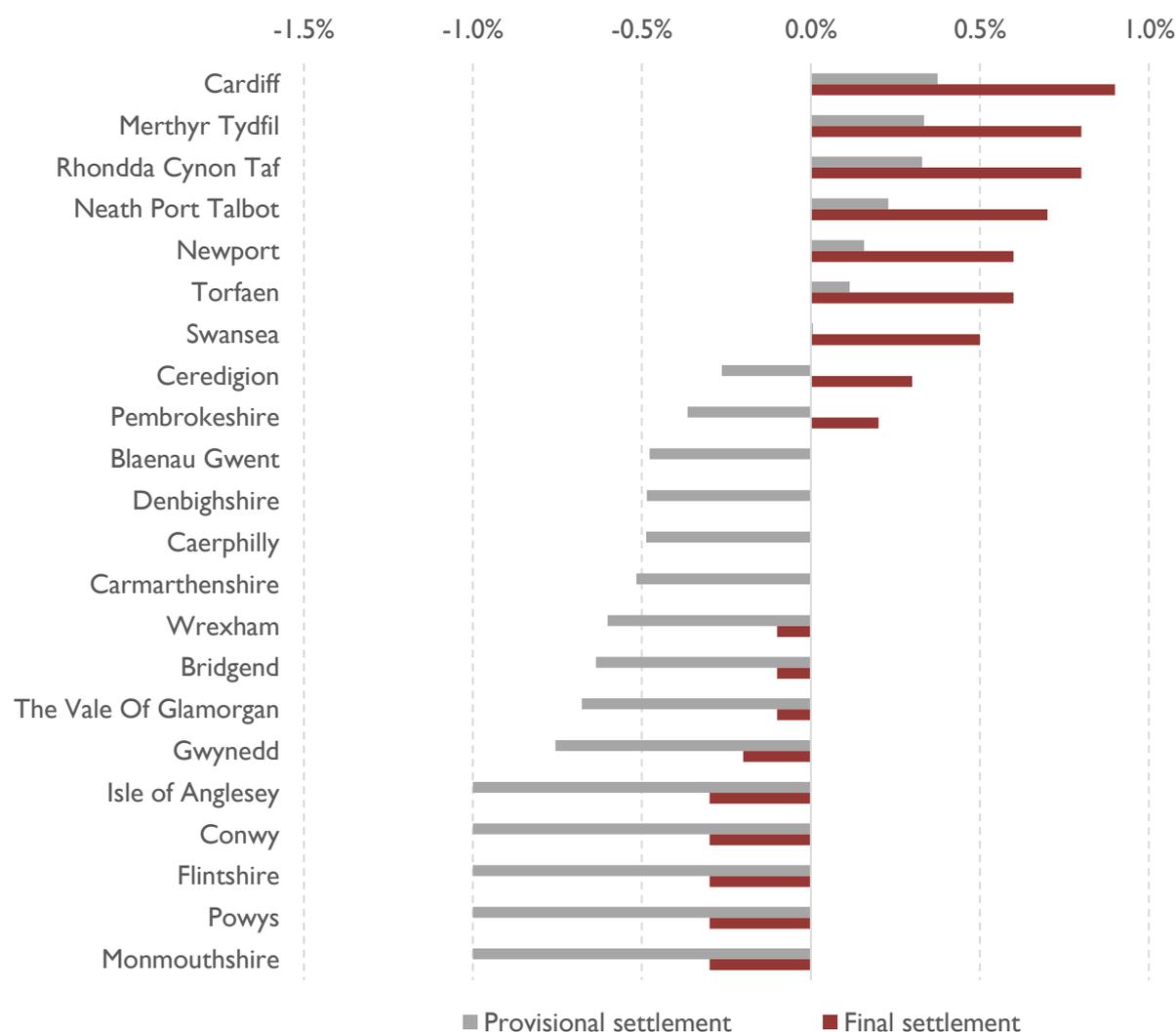
Local government

As outlined earlier, a large portion of the extra resource available to the Welsh Government since the Draft Budget has gone in to the local government settlement. At this time last year, local authorities were facing a 1% reduction (before inflation) in their revenue support grant from the Welsh Government. Allocations made in the Draft and Final Budgets has improved this picture significantly.

Figure 1 shows the change in aggregate external finance (which includes the revenue support grant) from 2018-19 to 2019-20 by local authority, comparing the provisional and final settlements.

Top up funding and additional allocations for social care mean that no local authority will face cuts of more than 0.3% in nominal terms next year. The number of local authorities facing a nominal terms cut in grant funding has fallen from fifteen in October to nine.

Figure 5: Change in Aggregate External Finance by local authority, 2018-19 to 2019-20 (nominal)



This year there is also significant additional funding for local authorities outside of the settlement. Most significant is the £30 million specific grant in the Health and Social Services MEG to address social care pressures announced in the Draft Budget.

Despite this additional funding however, budgets are still likely to be squeezed, with local authorities facing acute cost and demand pressures from public sector pay deals, increases to employer pension contributions, let along the ever present demographic pressures in the social care sector.

The funding allocated for the teachers' pay deal should cover most of the added costs for local authorities (though this is difficult to exactly assess). An outstanding concern for local authorities will be the increased costs relating to employer pension contributions. The UK government set aside £4.7 billion in reserve for 2019-20 to cover these pressures for all government departments, some of which will eventually be passed on to the Welsh Government.

We'll be looking at what this settlement may mean for council tax levels across Wales next month.

Looking across the UK, the cash-flat settlement for Welsh local authorities compares quite favourably to the settlements for England and Scotland. The announcement of increasing [core spending power for English](#) local authorities from their settlement broadly results from increased council tax revenues and masks a drop in central government support. In Scotland, [COSLA have argued](#) that there has been a cut to core budgets given the ring-fenced nature of new commitments in the settlement.

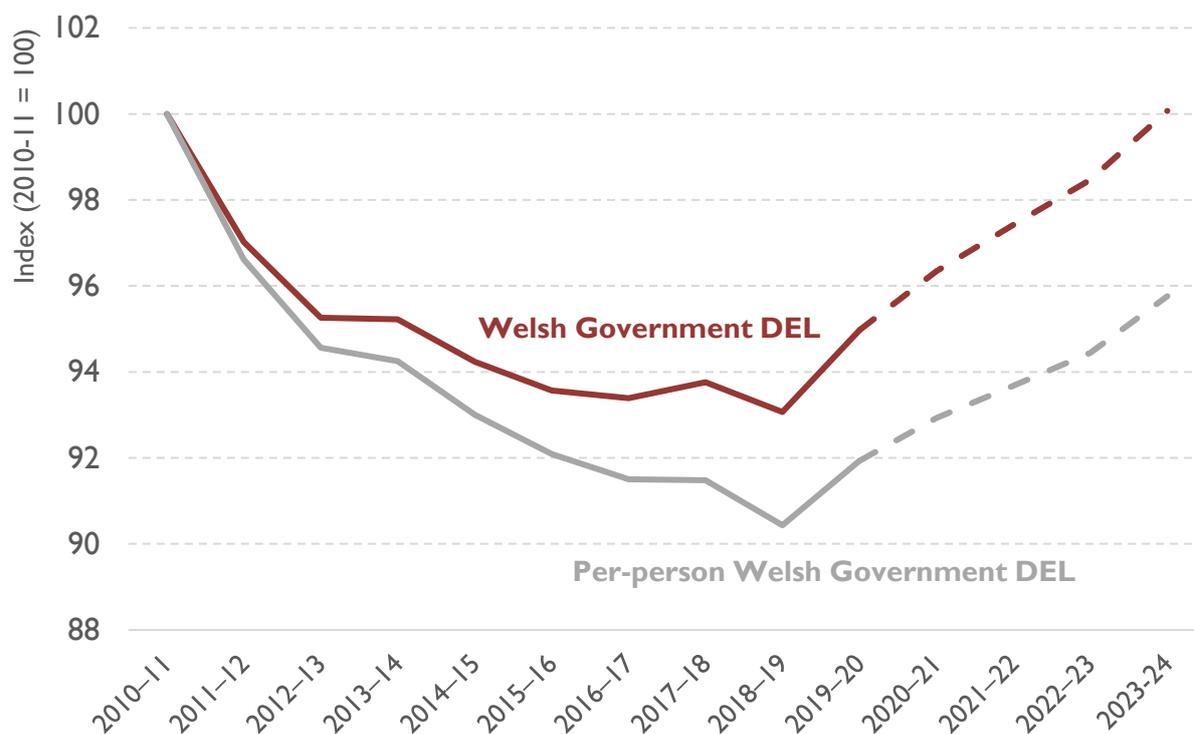
Outlook for future Welsh budgets

Given the context of political and economic uncertainty, the outlook for future Welsh budgets remains unclear. Since UK government departmental spending plans will not be published until the Spending Review next year, there is no firm path for public spending after 2019-20.

For now, we only have indicative plans after 2019-20 and Office for Budget Responsibility (OBR) assumptions. Total UK government day-to-day departmental spending will increase in real terms by around 1.2% in the years to 2023-24. Given the NHS funding deal in England and policy commitments to grow aid and defence budgets in line with national income, all other spending areas will essentially be flat in real terms.

If we assume funding increases will be shared equally across all other departments, we can use a crude Barnett calculator to work out the outlook for the Welsh Government day-to-day spending. Figure 5 shows this outlook based on these indicative plans, assuming the Welsh Government doesn't change its own tax policies and that Welsh tax performance keeps pace with block grant adjustments.

Figure 6: Real-terms changes in resource DEL (excluding depreciation), 2010-11 to 2023-24



The downward trend in the Welsh Government budget evident since 2010-11 looks likely to be reversed. It could be said therefore that austerity is indeed “coming to an end”. However, even after this increase in funding, on current plans it will still take until 2023-24 for day-to-day Welsh Government spending to reach its 2010-11 level in real terms. On a per-person basis, it will remain far below this level until significantly later in the next decade.

And, of course, this may yet turn out to be an optimistic scenario.

The extra spending announced by the Chancellor in October was largely paid for by large revisions in public finance forecasts by the OBR. Future revisions may not be so kind.

A ‘No Deal’ Brexit would significantly impact the UK economy and the public finances. The Chancellor Phillip Hammond has indicated that it would force an emergency budget, at which point spending plans for 2019-20 could be affected. Slower economic growth over future years could curb growth in spending over the next spending review period, unless the Chancellor’s fiscal targets are abandoned.

So, as with all private and public bodies this Christmas, the Welsh Government’s fiscal future remains in purgatory as Parliament sets the course for the UK’s exit from the EU in March.