

Briefing: public spending and austerity

October 2024

Introduction

In September 2024, chancellor Rachel Reeves promised “there would be no return to austerity” under the new Labour government,¹ echoing a promise made in the party’s election manifesto. Using data from the Office for Budget Responsibility (OBR),² this briefing note explores different definitions of austerity and calculates how much government spending would have to rise in the upcoming budget to fulfil Labour’s pledge to avoid austerity.

While politicians have been quick to blame austerity for the many challenges facing the public sector, there is a lack of clarity as to what the term means. When pressed as to what she meant by no return to austerity, Reeves answered that “there will be no real-terms cuts to government spending”.³ However, this definition of austerity is problematic as overall real government spending did not fall under the previous Conservative government either, contradicting Labour’s past criticism of austerity.

It is important to understand what the chancellor means by avoiding austerity as it is a key manifesto commitment that will constrain her choices on spending, which in turn has a significant impact on the public finances. A diluted definition of austerity would allow the chancellor to cut spending while still adhering to her manifesto commitment, although this would undermine past criticism of Conservative spending choices. On the other hand, remaining consistent with that past criticism would require a large increase in spending that will have to be paid for through higher taxes or borrowing.

Key findings

- If austerity is defined as **real-terms cuts to government spending**:
 - ◆ The chancellor could cut planned spending in 2025-26 by **£8.6 billion** and still claim to have avoided austerity.⁴
- If austerity is defined as **spending rising by less than under the previous Labour government**:
 - ◆ Planned spending would have to increase by **£40 billion** in 2025-26 to avoid austerity, this is **5.4 times** greater than the tax rises set out in Labour’s manifesto.⁵
 - ◆ Matching this rate of increase going forward would mean a total of **£394 billion** in additional spending by 2028-29.
- If austerity is defined as **public spending falling as a share of GDP**:
 - ◆ Planned spending would have to increase by **£13.1 billion** in 2025-26 to avoid austerity, this is **almost double** the revenue from tax rises set out in Labour’s manifesto.⁶
 - ◆ Maintaining public spending as a share of GDP going forward would mean a total of **£118 billion** in additional spending by 2028-29

¹ Smout, A, Macaskill, A, and Piper, E., *UK’s Reeves says no return to austerity in more upbeat economic message*, Reuters, 23 September 2024, www.reuters.com/world/uk/uk-finance-minister-reeves-vows-no-austerity-despite-tough-budget-2024-09-22/, (accessed 18 October 2024).

² Office for Budget Responsibility, *Public finances databank – September 2024*, 23 September 2024, obr.uk/download/public-finances-databank-september-2024/?tmstv=1729604024, (accessed 22 October 2024).

³ Guru-Murty, K., *Chancellor Rachel Reeves on UK economy, austerity and Labour gifts*, Channel 4, 23 September 2024, www.channel4.com/news/chancellor-rachel-reeves-on-uk-economy-austerity-and-labour-gifts, (accessed 18 October 2024).

⁴ All figures in this note are in 2023-24 prices unless otherwise stated.

⁵ Forecast revenue in 2028-29, Labour Party, *Change – Labour Party Manifesto*, 13 June 2024, p.127.

⁶ *Ibid*, p.127.

Defining austerity

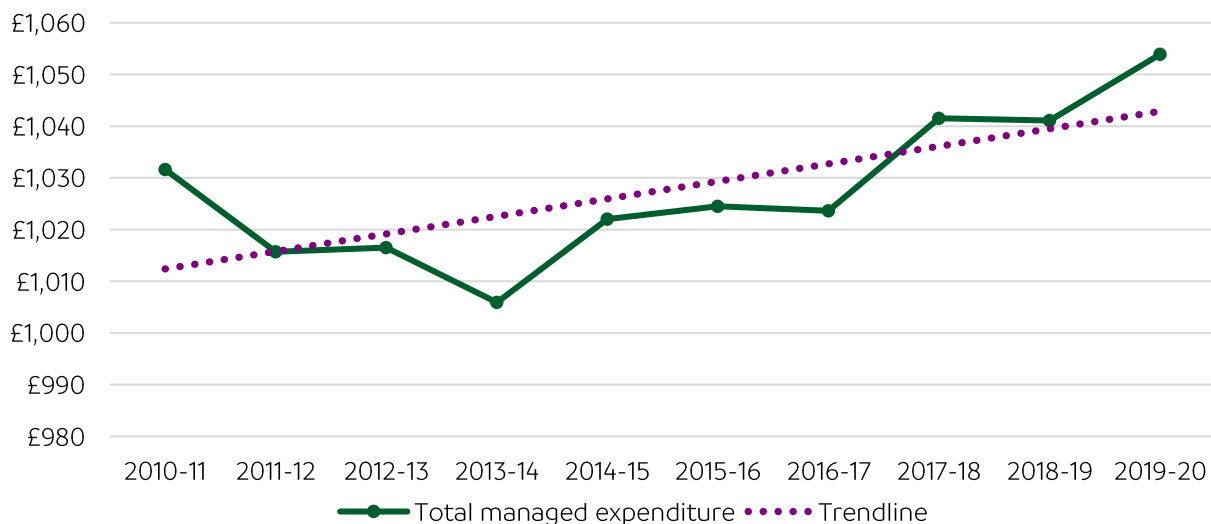
At its core, austerity refers to measures taken by governments to reduce debt – specifically reducing public spending or raising taxes. Under the previous Conservative government taxes did increase, supporting the austerity narrative. From 2010-11 to 2023-24, the tax burden was an average of 33.8 per cent of GDP. This is up from 32.6 per cent under the previous Labour government from 1997-98 to 2009-10, and 31.3 per cent under the Conservative government of 1979-80 to 1996-97. However, changes in spending, which for the purposes of this briefing note refers to total managed expenditure (TME), paint a different picture depending on the metric used. The following section will set out three different definitions of austerity and analyse how it affects the chancellor’s spending choices in the upcoming budget.

Option 1: austerity means real terms cuts to government spending

As previously discussed, this appears to be the chancellor’s current preferred definition.⁷ It is the definition that gives her the most room to manoeuvre when it comes to spending. Because total managed expenditure in 2025-26 is already projected to be £8.6 billion higher than 2024-25 in real terms, the chancellor could even cut spending by £8.6 billion and still be said to have avoided austerity under this definition.

Aside from the political difficulty of presenting an £8.6 billion cut as avoiding austerity, using this definition of austerity would seriously undermine Labour’s criticism of Conservative spending choices. Excluding the coronavirus pandemic which saw a sharp increase in spending, TME rose by an average of 0.24 per cent per year in real terms under the previous government from 2010-11 to 2019-20,⁸ meeting the definition of avoiding austerity seemingly articulated by the chancellor.

Chart 1: total managed expenditure, 2023-24 prices, £ billions, 2010-11 to 2019-20



Spending did fall by more than one per cent in real terms in two of the nine years (2011-12 and 2013-14), but this was more than made up for by increases in the remaining years. If austerity means real terms

⁷ Guru-Murty, K., *Chancellor Rachel Reeves on UK economy, austerity and Labour gifts*, Channel 4, 23 September 2024, www.channel4.com/news/chancellor-rachel-reeves-on-uk-economy-austerity-and-labour-gifts, (accessed 18 October 2024).

⁸ Office for Budget Responsibility, *Public finances databank – September 2024*, 23 September 2024, obr.uk/download/public-finances-databank-september-2024/?tmstv=1729254047, (accessed 18 October 2024).

cuts to spending, then austerity cannot be said to have occurred under the last government. Just prior to the pandemic in 2019-20, spending was some £33 billion higher in real terms than the peak under the previous Labour government. Despite rhetoric to the contrary, using this definition of austerity would mean the chancellor has committed to little more than a continuation of Conservative spending policy.

Option 2: austerity means real increases lower than under new Labour

To make the case that austerity occurred under the previous government, the bar for austerity needs to be set significantly higher. If the modest real term increases in government spending under the Conservatives constitutes austerity, then avoiding austerity must mean providing larger real term increases. The Darzi review of the NHS, for example, defined austerity as increases under the long-term average of 3.4 per cent.⁹ Specifically, the review points to one per cent real terms growth in NHS spending until 2018 as evidence of austerity.

A similar metric for overall government spending would be measuring it against past spending increases. Given their consistent criticism of Conservatives spending choices, it makes sense to compare both past and future spending to Labour's own record in government. This is a comparison that has been made by think tanks like the Progressive Economy Forum, which simulated how much higher public spending would have been in 2019 had it continued to grow at the same rate as under the last Labour government.¹⁰ Looking at the historical data, growth in public spending from 1997-98 to 2010-11 was considerably higher than under the Conservatives, supporting the austerity narrative. TME grew by an average of 3.99 per cent per year in real terms in this period, compared to just 0.24 per cent per year from 2010-11 to 2019-20.

Yet this definition makes the chancellor's pledge much more ambitious. If real spending growing by less than 3.99 per cent per year constitutes austerity, the chancellor will need to increase spending by at least 3.99 per cent in real terms to avoid austerity. TME in 2024-25 is expected to be £1.22 trillion, with spending expected to rise by a modest 0.7 per cent in 2025-26. Boosting that increase to 3.99 per cent would mean spending an additional £40 billion more than currently planned.

Table 1: increase in total managed expenditure necessary to avoid austerity (defined as increases lower than under new Labour), 2023-24 prices, £ billions, 2024-25 to 2028-29

Year	Current forecast		Necessary to avoid austerity	
	TME	Increase (%)	TME	Increase (%)
2024-25	1,216.6	-	1,216.6	3.99
2025-26	1,225.2	0.71	1,265.1	3.99
2026-27	1,241.3	1.32	1,315.6	3.99
2027-28	1,249.5	0.66	1,368.1	3.99
2028-29	1,261.5	0.97	1,422.7	3.99
Total spending	4,977.5		5,371.4	
Additional spending	394			

Table 1 demonstrates that increasing spending by at least 3.99 per cent per year going forward would cost a total of £394 billion more in spending by 2028-29. This rise in spending would need to be paid for either through higher borrowing or increased taxes, pushing the national debt and tax burden to unprecedented levels. This would make it extremely difficult for the government to keep their promise not to raise taxes on working people.

⁹ Department of Health and Social Care, *Independent investigation of the NHS in England*, 12 September 2024, p.7.

¹⁰ Calvert Jump, R., et al, *The Macroeconomics of Austerity*, Progressive Economy Forum, March 2023, p.20.

Option 3: austerity is shrinking the size of the state

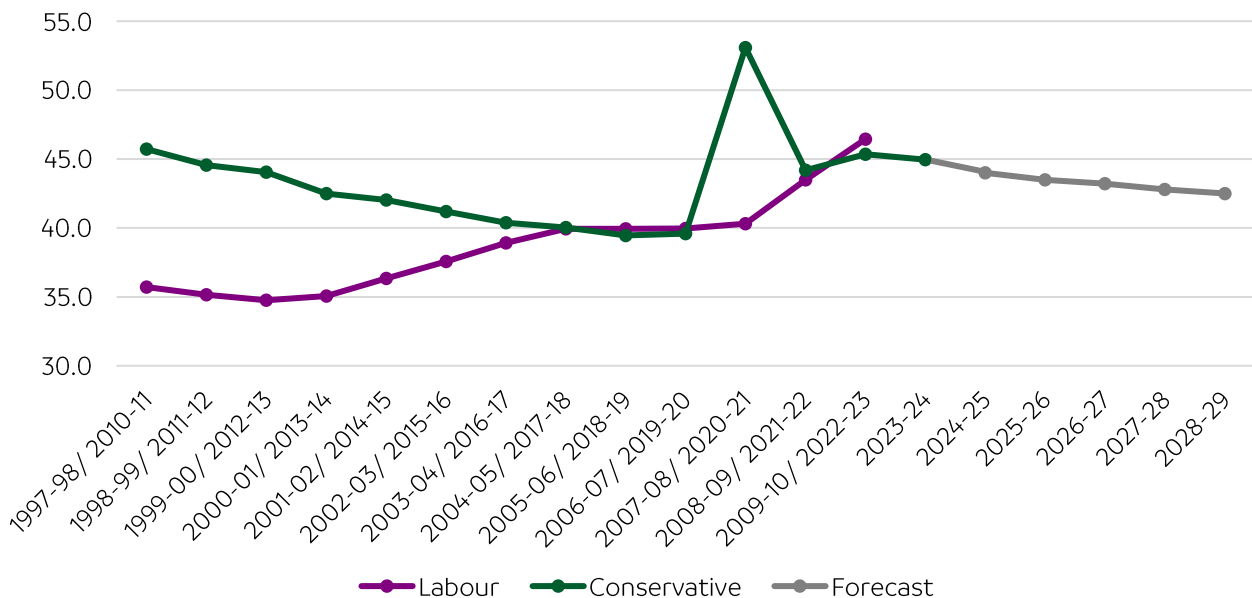
One argument against using past increases in government spending as the benchmark for austerity is that it does not consider the state of the wider economy. Average increases of 3.99 per cent per year were arguably only possible because of strong economic growth, with slower GDP growth since the pandemic making replicating past increases unrealistic.

Austerity, therefore, should be measured relative to the size of the overall economy. This approach aligns with what those close to the chancellor have said about austerity, namely that it was a “political choice with the ideological objective of a smaller state”.¹¹ On this view, government spending must not only rise in real terms but must rise enough to ensure that the state does not shrink relative to the rest of the economy. Austerity would thus have occurred if the state became smaller under the previous Conservative government. Yet the evidence for this is mixed.

Figure 2 below compares TME under previous Labour and Conservative governments. Spending as a percentage of GDP under Labour spiked in 2008-09, peaking at 46.4 per cent in 2009-10 before subsequently falling under the Conservatives. This downward trajectory continued until 2020-21 when spending once again spiked due to the pandemic. Significantly, even though spending as a percentage of GDP was on a downward trajectory under the Conservatives, the relatively high baseline meant that by 2019-20, public spending as a share of the economy had merely returned to pre-2008 levels.

Indeed, spending as a share of the economy was on average higher under the Conservatives than under Labour, even after excluding the pandemic years. Average TME from 2010-11 to 2019-20 was 42 per cent of GDP, compared to an average of 38.7 per cent of GDP under the previous Labour government from 1997-98 to 2009-10.

Chart 2: total managed expenditure (TME), per cent of GDP, 1997-98 to 2028-29



It is plausible that the chancellor is referring to the downward trajectory of public spending as a share of GDP following the global financial crisis when she talks about austerity. This trend is set to repeat

¹¹ Eaton, G., Will Rachel Reeves end austerity, *The New Statesman*, 23 September 2024.

post pandemic. TME has been steadily trending downwards since the height of the pandemic where it was 53.1 per cent. It is expected to fall to 42.5 per cent by the end of the forecast period, equivalent to what it was in 2013-14 – which would have been the midst of Conservative austerity under this definition. Avoiding austerity would therefore require arresting or reversing this decline.

This has implications for the chancellor’s upcoming budget. In 2024-25, total managed expenditure is forecast to be 44 per cent of GDP, falling to 43.5 per cent in 2025-26. To maintain spending at 44 per cent of GDP, the chancellor would have to increase real spending in 2025-26 by £13.1 billion more than currently planned. Maintaining spending at 44 per cent going forward would mean total additional spending of £118 billion by 2028-29 as demonstrated in table 2. This additional spending will similarly have to be paid for through either higher taxes or increased borrowing.

Table 2: increase in total managed expenditure necessary to avoid austerity (defined as public expenditure as a percentage of GDP shrinking), 2023-24 prices, £ billions, 2024-25 to 2028-29

Year	Current forecast		Needed to avoid austerity	
	TME	Of GDP (%)	TME	Of GDP (%)
2024-25	1,216.6	44.0	1,216.6	44.0
2025-26	1,225.2	43.5	1,238.2	44.0
2026-27	1,241.3	43.2	1,263.5	44.0
2027-28	1,249.5	42.8	1,285.8	44.0
2028-29	1,261.5	42.5	1,307.5	44.0
Total spending	4,977.5		5,095.1	
Additional spending	117.6			

Other definitions of austerity

It is important to note that there are more ambitious definitions of avoiding austerity than those set out above. While calls to end austerity often contain little more than vague references to greater public investment without specifying how much spending should rise by or who should pay for it, there have been some more detailed proposals. For example, the Institute for Public Policy Research has argued that ending austerity means addressing various “social deficits”. They suggest this could entail spending rising to 48.9 per cent of GDP, higher than the peak under the previous Labour government.¹² In order to pay for this, they suggest taxes could rise to 41.8 per cent of GDP,¹³ up from 36.5 per cent currently. This would mean spending increasing by £151 billion more than what is currently planned for 2025-26, with a corresponding tax increase of £144 billion in that year. The adoption of such measures, though admittedly unlikely, cannot necessarily be ruled out.

Conclusion

Avoiding austerity cannot simply mean avoiding real term cuts to public spending, as the chancellor has suggested. If that were the case, spending could be cut by a further £8.6 billion while still avoiding austerity. Notably, under such a limited definition, even the Conservatives could claim to have avoided austerity during their time in government. Alternative definitions of austerity result in fewer contradictions, however they mean that the chancellor will have to spend a lot more to avoid accusations of austerity. Matching the previous Labour government’s rate of spending increases would mean nearly £40 billion in additional spending in 2025-26 alone, while maintaining spending as a

¹² Quilter-Pinner, H. & Hochlaf, D., *Austerity: There is an alternative and the UK can afford to deliver it*, Institute for Public Policy Research, 18 April 2019, www.ippr.org/articles/austerity-there-is-an-alternative-and-the-uk-can-afford-to-deliver-it, (accessed 24 October 2024).

¹³ Ibid.

percentage of GDP would cost £13 billion in additional spending. This would be on top of already planned increases, meaning that it will add to the chancellor's £22 billion fiscal "black hole".¹⁴ With spending needing to rise by a total of anywhere from £100 billion to nearly £400 billion by 2028-29 to meet this commitment, there is a real risk of significant tax rises in the upcoming budget.

¹⁴ Edgington, T. & Reuben, A., *Is there a £22bn 'black hole' in the UK's public finances?*, BBC, 23 September 2024, www.bbc.co.uk/news/articles/cx2e12j4gz0o, (accessed 22 October 2024).