



The economic impact of MPs' expenses – a much larger cut in public spending by the next government than previously had seemed likely

My economics mentor and predecessor as the CBI's Chief Economic Adviser Sir Donald MacDougall used to remind me that **political events had economics consequences**. His favourite example was the UK's mid-60s balance of payments crisis, which he attributed to a considerable extent to Christine Keeler and the Profumo affair. His argument was that **the Profumo affair ended up delaying the 1964 election by a year which in turn meant two expansionary election Budgets** (in 1963 and 1964) and meant that the economy was badly overheating in the first Wilson administration, leading to balance of payments problems under the then fixed exchange rate regime.

It is in this spirit that I look at the MPs expenses scandal. It probably will not affect the timing of the election, since it is more likely merely to reinforce the unwillingness of Gordon Brown (or quite possibly a successor) to hold an election any earlier than the last day allowed under the Parliament Act.

But the public concern at the willingness of MPs to treat the public purse as a personal slush fund seems to me likely to spill over into concern about the scale of waste in government spending more generally. The latest OECD estimates on **public spending as a share of GDP show the UK with public spending at 47.7% of GDP for 2009 compared with an average of 46.9% for the euro zone and 42.0% for the OECD as a whole***. Obviously the economic outlook has deteriorated since these numbers were published last December but this should not have affected the *relative* position greatly. **In the year 2000, the UK spent 36.6% compared with the euro zone average of 46.3% and an OECD average of 39.1%. So in the past 9 years public spending in the UK has risen by 10.1 percentage points as a share of GDP (in other words the share has risen by more than a quarter - 27.6%)**. I would be surprised if many people feel that there has been a commensurate improvement in the volume or quality of UK public services either in absolute terms or compared with other countries.....

Until the past fortnight, I had expected that the incoming government (almost certainly under David Cameron) would have an early budget in July next year that would cut public spending significantly (though the actual reductions would be phased in) to bring the public finances back close to balance around the middle of the decade. **My instinct now is that the public will not be satisfied unless spending is reduced sufficiently for there to be real tax cuts, which would mean even larger cuts in spending.**

I suspect that it will take quite a number of years for the UK to achieve world class public sector productivity. **So to get public spending as a share of GDP down by as much as the public are likely to demand over a 5 year period it will probably be necessary to slaughter some sacred cows rather than simply focussing on cutting waste.**

*Source: http://www.oecd.org/document/61/0,3343,en_2649_34573_2483901_1_1_1_1.00.html

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