Autumn Statement 2014 - Inclusion response

The Chancellor has today delivered his Autumn Statement, with the Office for Budget Responsibility also publishing its latest forecasts for the economy and finances - including its first assessment of progress in meeting the new 'welfare cap'. Our analysis and response is below. This briefing covers: the latest forecasts and projections; the welfare cap; progress on welfare reforms; a new test for self-employed tax credits claimants; and a new tax break for employing apprentices.

Economic growth projections

The Chancellor made much in his statement to Parliament today that the Office for Budget Responsibility (OBR) had revised up its forecasts for Britain's economic growth. That is true for this year and 2015, but what the Chancellor failed to mention was that the OBR has revised down its forecasts for economic growth from 2016 to 2018. Overall by 2018, the OBR is now expecting the size of the economy to be slightly smaller by 2018 than it did at Budget time. The path for economic growth posited by the OBR is now very similar to the latest survey of independent forecasts from November 2014.

Fiscal Projections

The Chancellor emphasised that public borrowing this financial year was expected by the OBR to be lower than in 2013-14, contrary to the expectations of many economic commentators - and that the OBR was projecting public borrowing to fall between now and 2019-20. However again he failed to fully set out the comparisons with the Budget forecasts. There have been some methodological and statistical changes since the Budget which affect the projections for public borrowing. However, on a like with like basis, theOBR is now expecting higher public borrowing this financial year and next compared to its Budget projections.

For 2016-17 to 2018-19 the OBR's projections for public borrowing are very similar now to those set out alongside this year's Budget. The most striking feature of the OBR's forecasts are how much more optimistic they are than the consensus amongst independent economic forecasters for public borrowing from 2016-17 onwards. While the OBR expects a small fiscal surplus (negative borrowing) by 2018-19, the consensus forecast is for continued public borrowing of £24 billion in this year.

It is also notable that the OBR projects total public spending to reach its lowest level as a percentage of GDP for 80 years i.e. since the 1930s. Whether this is achievable or indeed desirable, especially in the context of greater post-war public expectations of the reach of the state, must be open to question.

Unemployment

The improvement in the labour market in terms of rising employment and falling unemployment has been very rapid in the last year or so, and faster than the OBR expected at the time of the Budget. In consequence, their Autumn Statement projections for the ILO unemployment rate are lower throughout the period 2014 to 2018 than they had anticipated at the time of the Budget. The OBR's unemployment projections are very similar to the consensus view amongst independent forecasters.

In our view, the projections set out by the OBR and the consensus may be slightly pessimistic. Despite the rapid recent declines in unemployment there are no signs of wage growth accelerating. We have previously noted that the rate of movement from one job to another remains well below pre-recession levels and this may be contributing to continued muted earnings growth. If so then there is scope for the economy to expand and for unemployment to fall further. It is not clear that this factor has been fully factored in by theOBR or other economic forecasters.

The welfare cap has been met, for now

The Office for Budget Responsibility has set out in its **Economic and Fiscal Outlook** its first assessment of the government's progress against its new overall welfare cap. We explained the cap at the last Budget. The key issue was whether spending on welfare benefits for people of working age, excluding JSA and Housing Benefit for those on JSA, was forecast to be within 2% of the amount predicted last year (a figure of around £2.4 billion a year).

The OBR's assessment is that spending will be within this 2% margin – with it being around 1% higher this year, falling to slightly lower than previously forecast by 2018/19. Underneath this, some forecasts have fallen while others have risen:

- On the one hand, falling inflation will reduce benefit spending by over £1 billion a year by the middle of the next Parliament, while "another delay to the rollout of universal credit" will save up to £1 billion a year. Delays to UC actually save the government money, as UC is marginally more expensive than the benefits that it replaces.
- On the other, the costs of delays to the rollout of the Personal Independence Payment and problems with the assessment of Employment and Support Allowance claimants are leading to extra costs of around £2 billion a year in the next Parliament.

Overall, without the surprising falls in forecast inflation since the Budget - and the less surprising delays to Universal Credit - the government would have been at risk of missing its welfare cap during the next Parliament. In our view, more than anything this goes to show that the welfare cap is a blunt instrument that fails to address the underlying drivers of social security spending.

The rollout of Personal Independence Payment may never achieve the savings expected

The Autumn Statement documents set out that changes to the "phased approach" to rolling out PIP will lead to savings being around £170 million lower over the next Parliament than was previously forecast. In addition, the OBR has "revised up the expected success rates" for PIP applications, reflecting their view that claimants are more likely to be successful than has previously been estimated. This further raises spending by around £400 million per year.

These adjustments do not, in themselves, represent any changes to the rollout or application of PIP. However they do demonstrate that the original savings assumptions, and the timetable for rolling out the reforms, were far too ambitious. It is welcome that this is now being recognised and corrected.

The backlog of Work Capability Assessments will take up to two years to clear

The OBR also sets out that, in its view, it will take up to two years to clear the significant backlog of WCAs that has built up under the Atos contract. The delays and backlogs that have built up are estimated to have led to additional costs of on average £700 million per year.

Getting back on track is predicated on Maximus, the new contract holders, hitting their target of up to 1.3 million WCAs a year. This will be a significant step up from recent years. However, Maximus will be supported in part through the recruitment of additional healthcare professionals – which, interestingly, are presented as a net saving to the Exchequer in the 'Policy Costings' published alongside the Autumn Statement.

A further freeze to Universal Credit work allowances.

The Autumn Statement also announces that 'work allowances' under Universal Credit will be frozen for a further year (2017/18). This follows the three years of freezes announced previously, covering 2014-17.

Work allowances are the amount of income that is ignored for households claiming UC. Freezing these allowances means that the amount of income ignored will fall, in real terms. So if a household's earnings rise, then their UC award will now fall by more than was previously expected. This will make low-income working households worse off by around £100 million a year, and will worsen the financial returns from moving into work or increasing earnings.

A new test of 'genuine and effective work' for self-employed tax credits claimants

The Autumn Statement announces a new test of 'genuine and effective work' for self-employed tax credits claimants who earn below the equivalent of 24 hours a week at National Minimum Wage. Alongside this, self-employed claimants of tax credits will need to register with HMRC and obtain a Unique Tax Reference.

This is presented as a measure to address "bogus self-employment" – where individuals claim that they are self-employed in order to access Working Tax Credit. However it is also likely to have implications for those supporting unemployed people to set up in self-employment (and in particular Work Programme providers).

An end to Employer National Insurance for young apprenticeships

Finally, the Autumn Statement includes one new employment measure. From April 2016, Employer National Insurance will be abolished for employers taking on apprentices aged under 25. Around 500,000 people start apprenticeships every year, however a declining proportion of these are aged under 25 (54% on the most recent data). This measure may serve both to increase apprenticeship take-up but also to redress this decline. **BIS research (PDF)** suggests that just over half of young apprentices were previously unemployed. So anything that reduces the costs of employing young people is, in our view, welcome. However as we have set out previously, it is unlikely that this measure on its own will have a significant impact on employment and unemployment.