Government austerity: Why the cuts are not necessary (Part1)

When presenting the Comprehensive Spending Review George Osborne said the unprecedented cuts were necessary because the country was "on the verge of bankruptcy". This was simply not true. The finances of a country are not like the budget of a household. The country would not be closed down and everyone asked to leave. In fact, When you look at the deficit in its historic context there is no basis for the scaremongering of the ConDem coalition.

Before the carrot of Cabinet posts was dangled before them the Liberal Democrats said that the additional cuts that the Tories were proposing threatened to throw the economy back into recession. The idea that the Lib Dems did not realise how bad the country's finances were is pure rationalisation to justify their support for a programme that they opposed before the General Election.

Despite all the rhetoric against the coalition, New Labour differs over the extent and pace of the cuts rather than on the need for them. The consequences of this current account deficit, which in absolute terms has never been as large (£156 billion in 2009/10), is being talked up by the coalition government. This current account deficit is presented by them as the result of New Labour’s profligacy. In fact a deficit can be viewed as a spending gap or a revenue gap. To see which it is you have to look at how the deficit emerged.

The tax expert Richard Murphy points out that the budget forecast for government income in 2008-9 was £608 billion. However, under the impact of the biggest recession since the 1930's government income sank to £496 billion; £112 billion less than expected before the 'credit crunch'.

The Treasury has seen a decline in the receipts which it receives from income tax, National Insurance, VAT and so on, as seen in the box below.

Income Tax	£8.4 billion in 2009/10 less than in 2008/9, £6.8 billion less than 2007/8
National Insurance	£2.1 billion less in 2009/10 than in 2008/9, £6.4 billion less than 2007/8
VAT	£8.3 billion less in 2009/10 than in 2008/9, £10.5 billion less than 2007/8
Corporation Tax	£7.3 billion less in 2009/10 than in 2008/9, £10.6 billon less than 2007/8
Capital Gains Tax	£5.3 billion less in 2009/10 than in 2008/9, £2.7 billion less than 2007/8
Petroleum Tax	£1.7 billion less in 2009/10 than in 2008/9, £0.8 billion less than 2007/8

Overall, receipts were down £35.4 billion from 2007/8 to £2009/10.

The deficit also, of course, includes the cost of bailing out the banks, and protecting the money of ordinary account holders. Late in 2009 The National Audit Office estimated that preventing a banking crash cost £850 billion. This included buying £76bn of shares in Royal Bank of Scotland and the Lloyds Banking Group; indemnifying the Bank of England against losses incurred in providing more than £200bn of "liquidity support"; guaranteeing up to £250bn of wholesale borrowing by banks to strengthen liquidity; providing £40bn of loans and other funding to Bradford & Bingley and the Financial Services Compensation Scheme; and insurance cover of over £280bn for bank assets. Nationalisation of Northern Rock alone added £100 billion to the national debt.

Mr Prudence

Although it’s a long time ago now, the 'Iron Chancellor', Gordon Brown, insisted on sticking to Tory spending limits for the first two years that New Labour was in office, to convince big business and the money markets of his “prudence”. Even the previous Tory Chancellor Clarke said he would probably have not stuck to such rigid spending plans. At any rate Government expenditure, which had been at 37.6% of GDP in the last year of the Major government sank to 34.5% in 1999/2000. *It was not until 2004/5 that as a percentage of GDP New Labour spending reached the level of the last year of the Major government*. Even in 2008/9 it was still under 40% (actually 39.4%). In contrast in the first 6 full years of the Thatcher government it was above 40%. So in real terms Brown was spending less than Thatcher at that stage!

If you look at the “Gross Nominal Liabilities of the National Loans Fund”, or national debt, you get a similar picture. After the Second World War national debt reached 252% of GDP yet this did not stop the introduction of the welfare state institutions. It was not until 1964 that the debt declined to below 100% of GDP, declining under both Labour and Tories.

In 1980 it was 46.2% of GDP. Despite Thatcher’s effort to “push back the boundaries of the state” it stayed above 40% until 1989. Under Major it was down to 34.4% but rose steadily to 52% in 1996. Under New Labour it declined to 41.1% in 2003.

It is of course true that a high level of annual deficit leads to a big increase in the cost of debt interest (an estimated ££44 billion in 2010/11). It is also true that such a deficit cannot be ignored. However, there are different ways of reducing the deficit. What the Tories have decided to do is to add an extra £29 billion of cuts *on top of* the £52 billion programmed in by New Labour.

The consequence of this ‘enhanced’ programme of cuts is estimated by the Treasury to be the loss of an additional 1.3 million jobs, 600,000 in the public sector and 700,000 in the private sector (the latter is the estimated impact of cuts in work carried out by private companies for the public sector - about 30% of public spending goes to private sector companies.). There are higher estimates. For instance, the Chartered Institute of Personnel and Development suggests 750,000 public sector jobs will go as a result of the government’s austerity measures. Either way, more than 1 million people are liable to be thrown onto the dole to add to the 2.45 million already there. To this can be added 1.07 million people who have taken part-time work because they cannot find a full-time job, though they would take one if they could. In addition, amongst the “economically inactive”, more than 2 million say they want to find a job. All of these have less than 500,000 job vacancies to chase after. In addition the government is seeking to push 1 million people on disability benefit onto Job Seekers Allowance.

The private sector to the rescue?

The assertion of the government that the private sector will create over 2 million jobs over the course of a Parliament has no evidential base whatsoever. Will Hutton points out that:

“According to accountancy firm PwC, Britain succeeded in generating 1.2 million private-sector jobs in the 1993-1999 recovery after the last big recession, but 900,000 of those were in financial and business services – which were hiring aggressively in the build-up of the credit and financial bubble. That cannot happen again on the same scale; in fact PwC forecasts 200,000 job losses in business and financial services up to 2015 from falling public-sector demand alone.”

It’s worth pointing out, however, that even if the dubious economic projections of the Treasury proved to be true, *by their own estimate* there would still be 1.9 million unemployed at the end of this period.

You can of course, tackle a current account spending deficit by increasing tax, but since Thatcher it has been economic orthodoxy that income tax rises were forbidden, because it would make a party unelectable. But this did not stop Tory and Labour governments increasing tax in a regressive way, especially with VAT which impacts more on the spending of the poor than the rich.

The coalition government budget cuts will serve only to *depress* economic activity and its own revenue, through the cost of increasing unemployment, and cutting government contracts, which parts of the private sector depend on. It is liable to increase government spending by increasing unemployment, just as Thatcher did. Whilst she changed the way that unemployment was measured (more than a dozen times), claimants were merely shifted onto disability benefit.

The budget cuts in relation to social benefits, including what Simon Hughes, Deputy leader of the Liberal Democrats, has called "draconian" housing benefit cuts, show the double standards of the government, which does not show the same determination to chase tax cheats as its does "benefits cheats". The latter are compared with "muggers", yet when it comes to financial institutions whose actions triggered the crisis, they are to be stung for a piddling £2.5 billion. We mustn't frighten them out of the country we are told.

Tax cheats and tax collection

When it comes to collecting the money that the government is owed, it does not show the same zealous attitude as it does to "benefit cheats". It is continuing what New Labour did when it got rid of 26,000 staff at the HMRC since 2005. 5,000 front line staff went last year and the coalition is looking to get rid of a further 15,000. It is hardly any wonder that the HMRC does not have the human resources to tackle the problems of tax avoidance (estimated at £25 billion a year in research he did for the TUC), tax evasion (estimated at £70 billion), and unpaid tax which the HMRC estimates at £26 billion.

A government minister has said it is losing £5 billion a year from benefit cheats. They cannot even read their own documentation correctly. He was conflating fraud and *errors*. In fact a report of the DWP gives their estimate of loss from fraud as £1.6 billion.

Richard Murphy's estimates are contested, of course. HMRC estimates a loss of £40 billion a year through tax avoidance and evasion. Yet even if you take the HMRC estimate as good coin, the government is losing roughly *25 times* what the DWP estimates is being lost to benefit fraud. As a government whose byword is "efficiency" why would you devote more resources to collect a sum one twenty fifth of that of lost tax revenue and continue to reduce the resources of the HMRC so that it cannot conceivably due the job of bringing in money which the government should receive?

Our cuts are better than yours?

Labour's last Chancellor, Alistair Darling, presented a budget which set itself the target of halving the current account deficit in 4 years. Should anybody have forgotten it, it is worth remembering that Darling himself said that this level of cuts would be deeper than those of Thatcher. "Hard choices", indeed. With the election of Ed Milliband as leader there was speculation as to what extent he would break with New Labour. He has made criticism of their policies in some respects, including their failure to regulate the banks sufficiently. Yet his appointment of Alan Johnson as Chancellor was not just a gesture to the uber-Blairite wing of the Party. As Milliband stated in his leadership speech at the Labour conference his "starting point" was the programme of cuts that Darling set in train. Darling's cuts add up to £52 billion over 4 years compared to Osborne's £81 billion. How can you mobilise your supporters in a campaign in favour of £52 billion cuts?

We are not opposed to all cuts, said Johnson, when questioned by the media. Yet in reply to the question of what cuts he did support, Johnson was evasive. Perhaps he is too embarrassed to say he is in favour of the £20 billion "efficiency savings" in the NHS. It's not a winner really, is it? But what's £29 billion between neo-liberals?

"Growth" or socially useful production?

A consistent challenge to the coalition government's austerity drive requires an alternative. Some of the elements of that can be found in Richard Murphy's work. But there is a missing element. This relates to the question of "growth". Amongst Labour politicians and many union officials the orthodoxy they share is that the way to tackle the deficit is "to return to growth". Yet growth, as currently conceived, is nothing other than an increase in economic activity (See http://martinwicks.wordpress.com/2010/03/24/trades-unions-and-economic-growth/). The concept takes no account of the social and environmental consequences of particular forms of economic activity. 'Growth' can in fact be a waste of human and material resources. It can have a detrimental impact on the environment. It can waste resources which could otherwise be spent on socially useful activity. What use is spending £80-100 billion on Trident renewal, a socially useless act, when you are butchering services which are provided to the poor and the under-privileged?

The key question which needs addressing is what sort of economic activity is socially useful, and in the interests of the majority of the population? To rely on 'the market' to create the number of jobs to stop the rise of unemployment and reduce it is self-delusion.

Whilst it might be argued that Darling's 'quantitative easing' package may have stabilised the position of the financial institutions, his free market prejudices meant that the 'nationalisation' of Northern Rock, RBS and Lloyds/HSBC was viewed as a pragmatic and temporary measure rather than as a means of 'rebalancing the economy' towards more socially and environmentally useful economic activity. The failure to take real control of the banks and make them invest in socially useful activity, such as council house building, or sustainable energy, is one of the reasons why unemployment has remained so high.

If they were going to spend £200 billion think what they might have done with it instead of giving it to the banks. They could have (leaving aside the possibility of expropriation) bought off all the PFI contracts, writing off the debt, taking the work and the staff back in house, so that hospitals were no longer under pressure to cut health spending because of the price of these glorified hire purchase schemes. They could have written off Council housing debt and invested in a mass Council house building programme and projects for alternative energy.

Parasitism, real and imagined

Isn't it ironic that behind the consensus on the need for public sector cuts is the idea that public services are parasitic on the 'real economy', when in fact, the global crisis has resulted from the very real parasitism of the financial sector. The globalisation of the finance markets created a situation where instead of finance providing money for investment in the economy (for producing commodities or services) the economy was increasingly subordinated to the interests of finance. The rapid growth of private equity was a good example, with acquisitions based on loading up companies with massive unsustainable debts (usually 80% of the acquisition price), but making big bucks for a few individuals very quickly. Just like Manchester United and the Glazers! Making money from money or from fictitious capital was so much easier than making it from traditional economic activity, with profit margins much higher.

In fact government spending creates the conditions for private industry to make a profit. Imagine if private haulage companies had to pay for the cost of the road network and the damage that their vehicles do to it. The double standards which dismiss state spending as parasitic, can be seen in the different attitudes held to road transport, as compared to rail. Spending on the road network has been viewed as necessary investment, whereas spending on the railways has been viewed as a subsidy. The former is in effect a subsidy to the private transport industry.

The big business society

The UK coalition government wants to turn the services provided by the public sector into commodities that are bought and sold. The inhumanity of such a perspective will become progressively clearer. Already they have succeeded in putting more than angry 50,000 students on the streets as a result of their proposal to deepen the education market.

As I have tried to do in this article we need to show that the argument that these draconian cuts are necessary is not only false, but it is cover for an ideological agenda for creating a 'small state'. Moreover, it is against the interests of a large majority of the population. The government has declared hostilities against an ever wider section of the population, especially the poor, the disabled, the disadvantaged. In adopting this 'big bang' approach they may have bitten off more than they can chew.

In the next part I will look at practical alternatives to austerity.

Martin Wicks

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