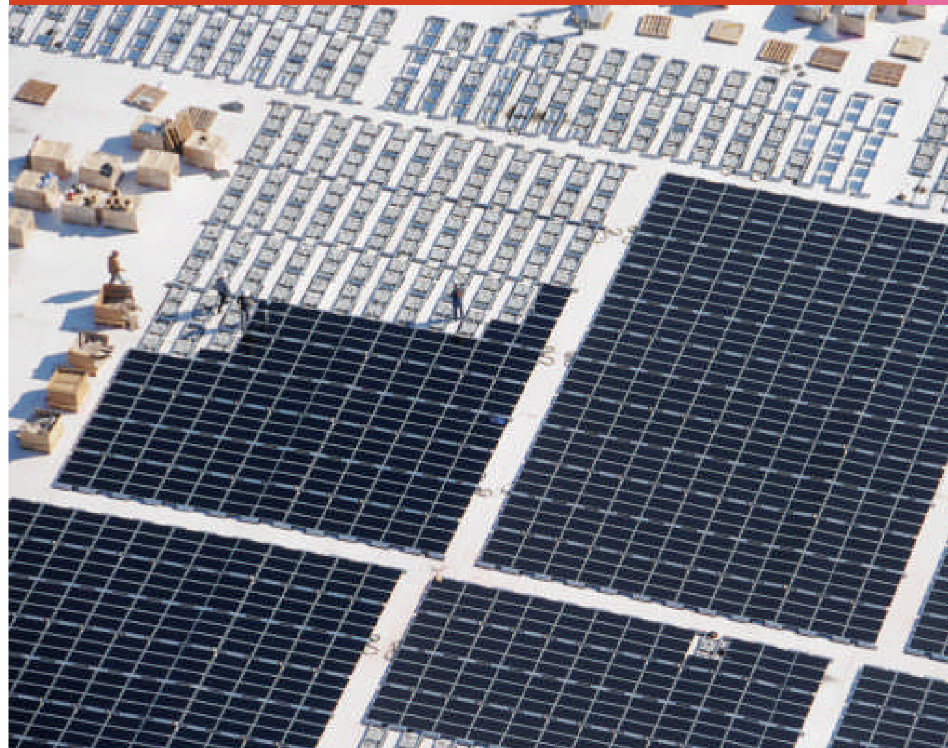
pwc.co.uk/ni

Northern Ireland Whatever Happened to the Programme for Government?

A critique of the Northern Ireland Draft Budget 2011-2015

March 2011



pwc

Contents

About Government Futures 03
Contacts 04
About this article 05
Whatever happened to the Programme for Government? 07
How good has our historic economic performance been? 10
What is the UK fiscal position? 11
And how does this read across to Northern Ireland? 12
The CSR – not swingeing cuts but challenging... 13
So where are we now? 14
Will the Budget 2011-2015 make any real difference? 15
What might a new Programme for Government look like? 18

About Government Futures

Welcome to our Government Futures series, in which we examine a range of public policy issues that are central to Northern Ireland's future prosperity and wellbeing.

On 15 December 2010, Finance Minister Sammy Wilson published the Northern Ireland Draft Budget 2011 -2015, much to the surprise of many observers who felt that some of the Executive would be distinctly uncomfortable putting their hands up for£4bn of cumulative spending reductions.

Nevertheless, the draft Budget was not only agreed for consultation, but it was agreed for the full four years of the comprehensive spending review (CSR) period rather than the 12 months that the Scots had opted for.

However, over succeeding weeks, the associated Departmental spending plans emerged piecemeal, without any common reporting format and, in the case of at least seven departments, without enough information for those participating in the consultation exercise to take a definitive view on their viability.

But perhaps the greatest disappointment was the absence of a new Programme for Government (PfG) against which the draft Budget and Departmental spending plans could be measured.

This was emphasised during the "take note" debate in the Department of Finance and Personnel Committee on 31 January 2011[1] where a Member suggested that "*the policy should inform the finance rather than the finance informing the policy",* while another remarked *"I do not know what the Budget is about. Is it just about getting through the next four years, or does the Assembly have any strategic vision?"*

In this publication we ask if the draft Budget and associated Departmental spending plans add up or if, in the absence of a PfG to inform the finance, this is a budget that simply gets Ministers and their officials through the next four years.

I trust you will enjoy this and our other *Government Futures* articles and find them a positive and constructive contribution to important debates about public policy and service delivery in Northern Ireland.

Paul Terrington
Public Sector Lead Partner
PwC Northern Ireland

[1] Committee for Finance and Personnel 16 February 2011, *Report on the Executive's Draft Budget 2011-15 Volume 1,* NIA 44/10/11R, Northern Ireland Assembly, Belfast.

Contacts

Dr Esmond Birnie
NI Chief Economist
PwC
E: esmond.birnie@uk.pwc.com
T: +44 (0) 28 9041 5808

Andrew Doherty
Senior Economist
PwC
E: andrew.doherty@uk.pwc.com
T: +44 (0) 28 90415751

Dr. Esmond Birnie is PwC's Chief Economist in NI. He was previously Special Adviser to the Minister for Employment and Learning (2007-10), an MLA (1998-2007) and Chair of the Assembly Committee for Employment and Learning (1999-2002).

As Senior Lecturer in economics in Queen's University Belfast (1999-2002) he was co-author of seven books on aspects of competitiveness, productivity and environmental outcomes of various western and eastern European economies.

Esmond holds economics degrees from Cambridge University and Queen's University Belfast.

Andrew Doherty is a Senior Economist with PwC. He has a strong background in quantitative and qualitative research methods, with a track record in providing economic analysis at local and central government level.

Previously, Andrew worked as an economist in the agri-food sector.

He has a Master's Degree in economics from the University of Manchester.

About this article

The Executive can no longer change the subject… the old Programme for Government will shortly pass its sell by date and a new one is nowhere to be seen.

On 25 October 2007, the then Northern Ireland Finance Minister, Peter Robinson, launched the Programme for Government 2008-2011, saying[2] *"now is the time for devolution to deliver."* Just minutes later, Deputy First Minister, Martin McGuinness, distanced the Executive from the policies of previous administrations by telling members that *"… this place is under new management."*

The new management had ambitious plans such that, by 2011, the Programme for Government (PfG) committed the Executive to *"… deliver a better and more sustainable future… a prosperous, fair and inclusive society, supported by a vibrant and dynamic economy and a rich and sustainable environmental heritage."*

The ambitions and objectives of the PfG 2008-2011 could be summarised by its five key priorities:

- Grow a dynamic, innovative economy.
- Promote tolerance, inclusion and health and well-being.
- Protect and enhance our environment and natural resources.
- Invest to build our infrastructure.
- Deliver modern high quality and efficient public services.

However, by 2010 the global financial collapse, recession and banking crisis had taken their toll on industry, exports – and the PfG. Addressing the Institute of Revenues, Rating and Valuation and the Chief Executives' Forum at Belfast City Hall on 3 June 2010, Finance Minister, Sammy Wilson, said: *"…over the next few years we will see massive reductions in public expenditure… we must rise to this challenge so that key frontline public services can be delivered in the best way…. the Northern Ireland Executive needs to decide what our real priorities are because we can no longer afford to deliver the full range of commitments set out in the Programme for Government."*

So, if the PfG, was deemed not deliverable (in terms of the full range of commitments) on 3 June 2010, one might reasonably ask, what has the Executive done in the intervening seven months to *"…decide what our real priorities are..?*

The draft Budget 2011-2015 and Departmental spending plans were produced, published and sent for consultation with little or no reference to the PfG 2008-2011 or any successor document. Little wonder, therefore, that a member of the DFP Committee remarked on 21 January 2011 in reference to the draft Budget and Departmental spending plans: *"I do not know what the Budget is about. Is it just about getting through the next four years, or does the Assembly have any strategic vision?"*

---

[2] Northern Ireland Executive 2007, *Building a Better Future; Programme for Government 2008-2011*, Belfast.

The Assembly rises on 25 March 2011; its members are already in full-blown election mode and, although the Budget was ratified by the Assembly on 9 March 2011, the process has resulted in a 2011-15 Budget being adopted without the electorate being fully informed or consulted on targets and outcomes for public services, economic rebalancing or social inclusion for the next four years.

The Executive can no longer ignore what has been obvious to many for more than six months – the old Programme for Government is unlikely to be delivered in anything like its entirety and a new one was nowhere to be seen during the draft Budget process.

The Scottish Executive published its interim Programme for Government in September 2010[3]. The Conservative /LibDem coalition was elected on 6 May 2010; they published their headline Programme for Government six days later and their full PfG on 31 May. The incoming coalition in the Republic of Ireland agreed their PfG in less than a week (27 February- 5 March 2011).

Both the Welsh and the Scots began their process well in advance of the Budget process and were therefore well prepared to produce meaningful PfGs. The Westminster and Irish coalitions faced articulate and influential economic critics and were emerging from an election process, as distinct from entering one.

Nevertheless, given a fortnight, the Northern Ireland Executive, in partnership with the private and voluntary sectors and the unions could agree a new, simple Programme for Government that would bring logic to the Budget process.

There is a way, but is there the will?

---

[3] Scottish Executive 2010, *Delivering for Scotland 2010. The Government's Programme for Scotland 2010-2011*, Edinburgh.

Whatever happened to the Programme for Government?

The Programme for Government 2008-2011[4] was, and remains, an ambitious and complex document, with 66 indicators used to inform the five key priorities and 331 indicators to inform the 23 public service agreements (PSAs), all of which were launched in what it described as *"… a more optimistic and promising era"*. Indeed, in the preceding year and as the Executive brought together their plans, they may have believed that their confidence was probably well founded.

The PfG commitment to develop "*…a vibrant and dynamic economy "seemed* to be on course; job-creation had been running at record levels; and, while house prices were rocketing (with some voices warning that they were out of control) there was a general acceptance that the eventual landing would be reasonably soft.

But that was not to be. When it received a PfG progress report on 23 June 2010, the Committee for the Office of the First Minister and the Deputy First Minister (OFMDFM) was advised that progress against the delivery of the five key priorities in the Programme for Government was mixed[5].

- Under the first priority – growing a dynamic and innovative economy – nine out of 17 key goals were on track (a 53% achievement).
- Under the second priority – promoting tolerance, inclusivity, health and well-being – 12 out of 17 goals were on track (71%).
- Under the third priority – protecting and enhancing the environment – five out of 11 key goals were on track (45%).
- Under the fourth priority – investing and building infrastructure – eight out of 11 key goals were on track (73%).
- Under the fifth priority – delivering high quality public services – four out of ten key goals were on track (40%) which was slower than anticipated.

On the face of it, the performance, at least in percentage terms, seemed fair enough. However, behind the 23 Public Service Agreements (PSAs), many of the 331 target indicators related to process events that were relatively easy for officials to achieve. Where there was meant to be a direct impact on social and economic outcomes, the achievement of the five key priorities was marginal.

In our PwC response to consultation to the PfG[6] we warned that the emerging fiscal challenges would significantly constrain both Westminster's and Stormont's public spending plans and that the deteriorating international situation would significantly reduce the volume of foreign direct investment (FDI) and depress prospects for indigenous growth and exports.

In that context we also argued that the PfG's targets were ambitious, but methodologies and strategies to reach them were unclear and, in some cases wholly absent. The target of halving the productivity gap with the UK average within seven years (when it had hardly shifted in the previous half century) was hopelessly naive, particularly in the absence of any meaningful strategy to deliver it.

[4] Northern Ireland Executive 2007, *op.cit.*
[5] Official Report (Hansard) 23 June 2010, OFMDFM Committee: Programme for Government: Delivery Reports, Northern Ireland Assembly, Belfast.
[6] PwC 2008, *Response to Consultation on draft Programme for Government, draft Budget and draft Investment Strategy*, PricewaterhouseCoopers LLP. Belfast.

Consequently, it is not surprising that there is considerable doubt as to the extent to which any real progress towards has been made towards delivering the first priority (growing a dynamic and innovative economy).

A recent PwC *Government Futures* report[7] suggested that 15 government-sponsored economic development reviews and strategies going back to the late 1940s had failed to close the productivity gap with GB. Furthermore, despite having created around 124,000 new jobs in the decade to 2008 – a remarkable performance and on par with US rates of job creation at that time, comparative productivity (relative to the UK average) actually fell to below where it had been in the mid 1980s.

NI's relative productivity and performance as a % of the UK

Sample sectors	1998	2008
Labour productivity (GVA per hour)	85.4	81.4
GVA per capita	79.2	78.9
Gross disposable household income	84.4	89.2
GVA as a % of total UK	2.3	2.3
GVA per job filled	88.0	84.0

Given the foregoing and the fact that historic information in respect of productivity and relative performance was in the public domain, it is genuinely difficult to understand how the PfG authors believed that some of the objectives, particularly around the economy and public sector modernisation, were to be achieved.

Effectively, therefore, under the first PfG priority – *growing a dynamic and innovative economy* – where the OFMDFM Committee was told in June 2010 that nine out of 17 key goals were on track (a 53% achievement), the key objective of halving the productivity gap with the UK has not been delivered. Indeed the gap is wider now than in the late 1990s. And adding to the problem, since the foundation of Northern Ireland in 1921 the only periods when the local economy showed any shift towards convergence with the rest of the UK were those where there were disproportionally high levels of public expenditure growth such as during the second World War and the height of the civil unrest in the 1970s and early 1980s.

One might therefore reasonably conclude that, in the absence of a dynamic, high-GVA private sector, the first PfG priority (*growing a dynamic and innovative economy)* cannot be delivered. It is possible to apply similar analysis to the other four PfG objectives. It is difficult to rationalise that, for example, because eight of 11 key *investing and building infrastructure* goals were on track at 73%, we are on the verge of delivering the objectives of the Investment Strategy for Northern Ireland (ISNI), when the reality is that the absence of anticipated public sector funding has brought the planned infrastructure programme almost to a standstill.

[7] PwC 2010, *op.cit.*

The reality is that there is little real evidence that the explicit planned outcomes of the PfG are even on track, let alone close to delivery. Consequently, in the absence of radical change, or an attempt to articulate a clear and deliverable strategy, the cumulative £4bn cut in public spending over the next four years will have a negative effect on any progress that has been made thus far.

So, looking to the future, there is little value in rolling over the PfG 2008-2011 for another four years and little value in creating a new PfG 2011-2015 that does not dramatically realign the economy, create significant private sector growth and dramatically reduces the size and cost of the public sector – without compromising service outcomes.

In conclusion, we warned[8] that without a clear vision, an agreed strategy (including partnership between public , private and third sectors) and dynamic leadership, the PfG would be doomed to share the fate of *"…many historic economic strategies [which] have failed to translate into objectives, let alone outcomes and have become little more than devices to tinker with the status quo."*

---

[8] PwC 2008, *op.cit.*

How good has our historic economic performance been?

Since 1921, Northern Ireland has failed to achieve sustained economic convergence relative to the UK average levels of GDP per capita and continues to languish at 80% of the UK average.

The argument that radical action is needed to rebalance the economy is supported by a recent PwC *Government Futures* report[9] that concluded that half a century of reviews and strategies had made no substantive improvement to the region's productivity and competitiveness. Indeed, in the ten years to 2008, while Northern Ireland created 124,000 new jobs, comparative productivity (relative to the UK average) actually fell to below where it had been in the mid 1980s.

The figures presented in Isles and Cuthbert [10], for example, suggest that relative income per head in Northern Ireland compared to the UK average jumped from only 55 % in 1938 to about 67% in 1942 and then stabilised at that level[11].

There was to be no sustained improvement on the mid Second World War comparative position until the mid 1970s and things have stood still over the last three decades. It is striking and depressing that the only periods when the Northern Ireland economy has managed any substantial move towards convergence with the rest of the UK have been ones when there was a very rapid increase in public spending; first of all during the Second World War and then during the early phase of the Troubles.

Given this correlation between high levels of public spending and economic activity, the cumulative £4bn fall in public spending over the period of the draft Budget does not auger well for the economy. In addition, the hitherto underestimated reliance on economic activity in the Republic of Ireland (RoI) will further impact on Northern Ireland's economic performance until RoI experiences significant recovery.

---

[9] PwC. 2010, *Business as Usual? The need for radical change to the delivery of economic policy,* Government Futures Publications, PwC, Belfast.
[10] K.S. Isles and N.Cuthbert 1957, *an Economic Survey of Northern Ireland*, HMSO, Belfast.
[11] Isles and Cuthbert, *op.cit.*

What is the UK fiscal position?

In the aftermath of the 2010 general election, a priority of the coalition government was to reduce the budget deficit which was about £150bn in 2009/10. The emergency Budget of 22 June set out plans to cut the deficit, with the Chancellor announcing £17bn of spending cuts by 2014/15, in addition to the reductions in spending which had been planned by the previous Labour government.

The outcome of the 22 June Budget was that public spending was forecast to fall in real terms for each of the next four years. To put this in context, public spending fell in real terms in only five years in the four decades between 1970 and 2010 and, over that period, public spending declined for two consecutive years on only one occasion (1996/97-1997/98).

At the same time, despite the cuts announced in the emergency Budget, public spending as a share of the economy in 2015/16 will still be higher than it was in 2003/04.

The underlying objective of the 22 June Budget was to cut the structural budget deficit to zero over the following five years. This was to be achieved through a combination of taxation and public spending restraint, intended to deliver an additional fiscal consolidation of around £40bn by 2014/15, over and above the measures included in the (pre-election) Budget of March 2010.

The consolidation was heavily weighted towards spending cuts rather than tax rises – with a ratio close to the 4:1 promised by the Conservatives prior to the election.

The Budget statement also included a restatement of the commitment contained in the coalition Programme for Government to publish by autumn 2010 a *"…paper examining potential mechanisms for changing Corporation Tax in Northern Ireland*[12]*."*

This commitment has been the subject of considerable recent argument, but, while this has concentrated on the merits (or otherwise) of reducing Northern Ireland's Corporation Tax rate to 12.5%, it has failed to fully develop the potential benefits of having tax varying powers, as distinct from the power to vary a single tax. We return to this important and neglected argument later.

[12] The Coalition May 2010, *op.cit.*

And how does this read across to Northern Ireland?

The implications of the 22 June Budget statement were in addition to the £6.2bn of public spending reductions announced for 2010/11 by the coalition the previous month.

In May 2010 the Northern Ireland Executive's share of these reductions amounted to £127.9m[13]. And while this was mostly managed through the in-year monitoring process, there was an option for the Executive to carry forward the reductions into 2011/12. On 29 September 2010 DFP officials gave evidence to the Finance and Personnel Committee where an official stated: "*As we leave September monitoring, the position is that the over commitment is cleared on the capital side, and we still have a balance of just under £17m of an over commitment on the current side."*[14]

That left the Executive to find an additional £17m in the remaining monitoring rounds of 2010/11 (December and February) if there was to be no carrying over of over commitment into 2011/12. Assuming the Executive was to find the £17m, it would start the next fiscal year with a clean slate.

On 20 October 2010, the Comprehensive Spending Review (CSR) set out UK departmental spending limits for the four years until 2014-15 whereby public spending as a percentage of GDP will return to the level seen in 2006-07, and in real terms it will return to around the level seen in 2008-09.

The CSR increased the capital envelope by £2.3bn a year by 2014-15 relative to the March 2010 Budget plan. And, for the first time, the CSR covered Annually Managed Expenditure (AME) in addition to Departmental Expenditure Limits (DELs) for each government department and the devolved administrations.

[13] DFP Press release 25 May 2010, available online at: http://www.northernireland.gov.uk/news/news-dfp/news-dfp-25052010-wilson-cut-in-public-spending.htm

[14] http://www.niassembly.gov.uk/record/committees2010/FinancePersonnel/100929_OutcomeofSpendingRound.htm

The CSR – not swingeing cuts but challenging…

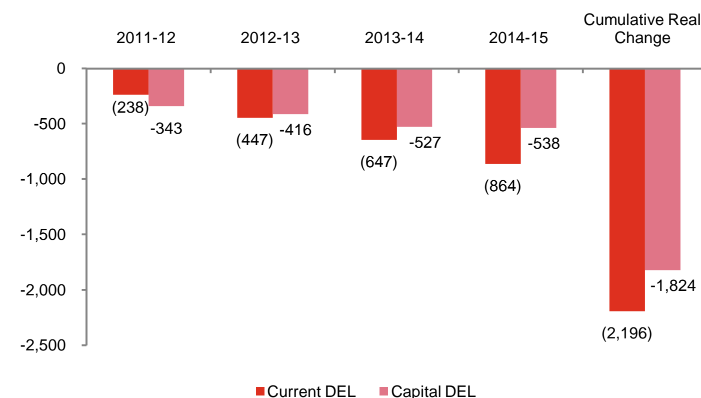
The Comprehensive Spending review (CSR) provided the immediate context for the Northern Ireland draft Budget 2011-15, and the settlement for the Northern Ireland Executive shown in Figure 1. Comparing 2014-15 to 2010-11, there was an 8% real terms decrease in the total monies allocated to Departmental Expenditure Limit (DEL) current expenditure[15] and a 40% decrease in the monies allocated to DEL capital expenditure[16] over the four year period.

DEL capital expenditure is the money used to provide infrastructure projects e.g. road building, upgrade of the water and sewage systems, hospital buildings.

The total cuts over this period represent a cumulative real terms decrease of £4bn compared to the baseline in 2010-11. The 15 December 2010 draft Budget document comments: *"While the level of reductions faced by the Northern Ireland Executive is lower than that faced by many Whitehall departments, it still represents a significant challenge for the Executive"*. [17]

Figure 1: NI total Departmental Expenditure Limit spending allocation from The Spending Review.

£m real terms reductions relative to 2010-11



---

[15] DEL current expenditure is the money that is used to provide the services of government Departments and includes staff costs and operating costs of providing those services.
[16] DEL capital expenditure is the money used to provide infrastructure projects e.g. road building, upgrade of the water and sewage systems, hospital buildings.
[17] DFP 15 December 2010, *Draft Budget 2011-15.*

So where are we now?

Since the CSR, there has been a steady improvement in the overall UK fiscal position, with January reflecting the highest monthly borrowing surplus since 2008, according to figures published from the Office for National Statistics (ONS). UK Public Sector net borrowing (excluding financial interventions) showed a surplus of £3.7bn last month, a dramatic turnaround on last January's deficit of £1.3bn.

Were that trend to continue, the coalition government could be on track to achieve its full-year fiscal target, although it should be remembered that January is the deadline for paying a number of taxes like Self Assessment and Corporation Tax, so it is generally a good month for receipts.

Nevertheless, the January figures show better than expected tax revenues and leave the deficit for the first ten months of the fiscal year at £113bn – around £14bn lower than last year. If the government can sustain this trend, and we don't see a reversal in February, total borrowings for the year could be around £10bn below the Office for Budget Responsibility's £149bn forecast.

However, while there is clear evidence of recovery, including improved manufacturing and export activity in GB, the Northern Ireland economic performance remains worryingly lacklustre. January's latest assessment of private sector activity[18] in Northern Ireland showed a further sharp fall in private sector activity as new business continued to decline, job shedding persisted, while strong cost inflation pushed up output prices for the first time since September 2008.

The rate of decline in overall business activity continued for the 38th consecutive month, with the construction sector experiencing the steepest drop in output and, while the rate of decline in manufacturing output was relatively modest, it continues to decline nonetheless.

Private sector employment fell in January, for the 33rd consecutive month. Construction and retail saw the fastest declines in workforce numbers, while manufacturing employment was broadly unchanged. Northern Ireland unemployment (Labour Force Survey) increased to 8% in Q4 2010, with a further 600 claimants recorded in January 2011. Northern Ireland's unemployment is now above the UK average (7.9%) for the first time in over five years and is at the level last experienced in Q3 1998.

In summary, therefore, the prognosis is poor. There is clear evidence of international recovery (subject to future commodity price volatility)with global growth back around the 3.2% historic trend, the GB economy is improving slowly and public borrowing is falling in line with the OBR forecasts. Northern Ireland however, remains mired with growth in 2010 estimated at around 0.8% and forecast growth for 2011 as 1%, at best.

---

[18] Ulster Bank February 2011, *Purchasing Managers' Index©*

Will the Budget 2011-2015 make any real difference?

It is encouraging that the Executive reached a consensus in December in terms of putting the Budget out to consultation and, in that regard, Ministers and their officials are to be congratulated. However, while the degree of political consensus already achieved is welcome, the way this process has been managed by individual Departments, their Ministers and the Executive does not inspire confidence that the Budget can or will be successfully managed through to implementation.

The draft Budget was delivered to the Assembly by the Finance Minister on 15 December 2010, but it was made clear that consultation would be managed not by DFP but by individual Departments. The Minister said: *"...This process will not be led by DFP but by individual Departments who will now publish their savings plans and spending proposals. This will allow interested parties to provide the views that will shape the final Budget position that I will bring before this Assembly in February."*

This implied that Departments could *"... publish their savings plans and spending proposals"* in a manner of their own choosing. We believed at the time that this could result in a lack of transparency and an inability to compare Departments in a like for like manner. We believed this would be true especially in terms of relating individual Departmental spending and savings proposals, both to each other and to the draft Budget statement of 15 December. This has proved to be the case.

Furthermore, even with an extension to 16 February, the delay in the publication of Departmental plans left consultees with little time to rigorously scrutinise these plans. It also means that the Executive has almost no time to consider the responses. The publication by DHSSPS of its McKinsey Report (on around 10 February) containing estimates not in the DHSSPS plan was particularly challenging as it was (and remains at the time of writing) difficult to determine if the two documents collectively comprise the Health Department's Budget plan.

In overall terms, we conclude that the draft Budget (as defined by the published plans of the 12 Departments) does not balance. A calculation based on a standard formula (Departmental baseline plus inescapable as compared to resources plus savings) suggests that, in the absence of information not currently available to consultees, there is a cumulative shortfall that could exceed £2.0bn by 2014-15.

And while we understand that the Finance Minister found an additional £450m, which was announced on 3 March, we remain highly sceptical as to whether the Budget that was finally put to the Assembly will either balance or be capable of delivery.

We note that to a large extent Departments have not exercised opportunities to raise revenues and/or effect savings where opportunities exist to market test a wide range of services currently provided within the public sector. We would have expected Departmental proposals to show much greater imagination around ways to externalise service delivery, to dispose of publicly held assets and operations and to consider more radical mechanisms for finance-raising and asset-leveraging to fund essential infrastructure investment.

We have also identified a number of areas where cross-departmental activities may conflict. For example, an examination of the plans for the Desertcreat College suggests that, while sufficient capital may be available from DOJ to complete the campus, DHSSPS has insufficient resources to fund its proposed share of revenues costs. And we note the further deferral of domestic water charging will have the effect of subsidising DRD to the extent of around at least £800m over the period of the draft Budget.

There is an absence of adequate attention on what the Committee for Finance and Personnel calls "preventative spending".[19] In others words, pre-emptive spending on early policy interventions to ensure that more substantial public funding is not required in the future. Examples could include spending on early years/childhood to prevent today's young people becoming tomorrow's offenders or illiterates or drug and alcohol abusers.

We should acknowledge that the longer term benefits of preventative spending will, in the main, fall outside of the Budget period. Preventative spending needs to be balanced by a range of cross cutting strategies to address the current huge drain on resources and the major social issues which currently do not work through to sustainable outcomes.

We are therefore deeply concerned at the almost complete absence of economic and social targets and outcomes underpinning the draft Budget and Departmental plans for the period to 2014-15 and believe that the draft Budget and associated Departmental spending plans have more to do with 'getting through the next four years' than driving holistic policies intended to stimulate economic regeneration and social inclusion.

It is both striking and depressing that the only periods since 1921 when the Northern Ireland economy has managed any substantial move towards convergence with the rest of the UK have been ones when there was a very rapid increase in public spending.

It is therefore worth remembering that, based on the 22 June UK Budget, public spending is forecast to fall in real terms for each of the next four years. However, public spending fell in real terms in only five years in the four decades between 1970 and 2010 and, over that period, public spending declined for two consecutive years on only one occasion (1996/97-1997/98).

Given this correlation between high levels of public spending and economic activity, the cumulative £4bn fall in public spending over the period of the draft Budget does not auger well for the economy. In addition, the hitherto underestimated reliance on economic activity in the Republic of Ireland will further impact on Northern Ireland's economic performance until RoI experiences significant recovery.[20]

We are therefore facing an unprecedented public sector spending round. Also, one where the OBR UK growth estimates that informed the 22 June Budget have since been marked down. And one where Northern Ireland remains the single UK region not to demonstrate any real measure of recovery. Consequently, the Executive should not underestimate the potential for public spending to become even tighter over the current CSR period.

We would temper our criticism of the Budget and Departmental plans by commenting that the lack of holistic, cross-departmental cohesion in the plans is, at least in part, understandable given the multi party, 'enforced coalition' model of government.

A tight budget is difficult enough to deliver across Departments in a 'traditional' model of democratic government and this is significantly exacerbated by the political situation in Northern Ireland. However, the speed of progress in Northern Ireland towards getting a PfG in place alongside a Budget appears glacial when compared to Scotland, a minority government, or London or Dublin, both two party coalitions.)

[19] Committee for Finance and Personnel 16 February 2011, *op cit.*
[20] For example, 10% of manufacturing output is sold to the Republic of Ireland.

Nevertheless, the Budget, including the Departmental plans, comprises a patchwork of unaligned spending proposals. There is, for example, no sense of the need to be radical in terms of asking the question how far should the public sector itself provide service delivery and how far should it commission delivery from either the private sector/voluntary and community sector?

The Budget is largely unrelated to a PfG or to cross-departmental economic or social objectives and when a new PfG is formed there is no stated Budget Review mechanism to provide mid-term adjustments during the spending review period[21].

In fact, based on the information available, the Northern Ireland Budget may not be deliverable in its current form.

---

[21] A criticism also made by the Committee for Finance and Personnel 16 December 2011, *op.cit*. The generally much reduced sums which are now likely to be available through in-year Monitoring (which reflects the general success of the Departments in reducing under-spend) implies that in-year bids cannot really be used as a *de facto* mechanism to revise the Budget

What might a new Programme for Government look like?

Certainly not like the old one. That document, which had 66 indicators to inform the five key priorities and 331 indicators to inform 23 public service agreements (and which shows a 53% achievement for a key indicator that was demonstrably deteriorating) was not realistic.

There is little doubt, and the Executive would probably agree, that they must focus the reduced resources of the Budget towards economic regeneration, wealth creation and increasing the efficiency of service delivery, while significantly reducing the cost (and potentially the size) of government. We would expect this to be a clear priority in the draft Budget and in any new Programme for Government.

Neither do we accept that rolling over the old PfG 2008-2011 for another four years is an acceptable or realistic option. The clear lack of correlation between performance as perceived by officials and actual delivery of the five key objectives[22] is surely evidence that the old process is fatally flawed.

The coalition's much anticipated paper on Corporation Tax is still to be published[23] and in the absence of any significant move towards designating Northern Ireland (or parts thereof) as an Enterprise Zone[24] the region lacks any unique factor(s) that would deliver a step change in economic activity. And while we believe that a significant reduction in the level of Corporation Tax in Northern Ireland could be advantageous in attracting new foreign direct investment, we have calculated that the inevitable cost to the region could be disproportionate.[25] We believe that obtaining broader tax varying powers (which would include the power to vary Corporation Tax) would offer greater flexibility at less cost, but obtaining such powers could be subject to European Union approval and obtaining such agreement could take a prolonged period of time.[26]

However, that is not a reason for failing to make the devolution of tax-varying powers a priority in a new PfG as any new measures to make the Northern Ireland economy more competitive must attract significant levels of FDI, while stimulating increased productivity, exports and international competitiveness amongst both FDI and indigenous businesses.

Most research suggests that, as compared to indigenous undertakings, FDI brings to the host region higher levels of productivity, greater capital investment and more highly skilled labour opportunities. So, only by targeting and delivering FDI that significantly outperforms the median will the Northern Ireland economy begin to rebalance from public sector dependency to private sector dominance.

---

[22] OFMDFM Committee 2010, *op.cit.*
[23] Although a draft arrived with the Executive just before Christmas 2010.
[24] The Coalition May 2010, *op. cit*
[25] PwC 2011, *Corporation Tax: Game Changer or Game Over?,* Government Futures Publications, PwC, Belfast.
[26] PwC 2011, *op.cit.*

The *Independent Review of Economic Policy* (IREP)[27] suggested that many Invest NI-supported investments have been in relatively lower value added sectors, with only 46 percent of new FDI service jobs in the mid 2000s paying salaries above the NI private sector median.[28] IREP pointed, in particular, to contact centres, where only around 33% of new FDI jobs were above the NI private sector median. However, whilst IREP's analysis is accurate and provides a valuable basis for analysing past shortcomings, it offers no clear strategy towards radical change, nor does it offer suggestions as to where resources should be prioritised.

An added complication is that, from January 2011, changes to EU State Aid rules will reduce the maximum assistance that Invest NI can provide to companies in respect of regional aid (principally Selective Financial Assistance but not including R&D and training grants), further complicating the creation of appropriate incentives for FDI that will operate in the high productivity/GVA per capita sectors.

Consequently, to adequately recognise where resources should be prioritised, any new strategy emerging from IREP and which is translated into a new PfG should seek to identify and attract organisations, whether in the manufacturing or tradeable service sectors, which:

- pay salaries above the NI private sector median
- can generate labour productivity levels (GVA/hour) above the NI average
  hence
- generate GVA per capita above the NI private sector median
- deliver GVA per job filled above the NI private sector median.

Only by targeting and delivering FDI and indigenous investment that significantly outperforms the average can we begin to rebalance the economy; and if the price of attracting such investment is a penalty on foregone tax, that element too, should be factored into the mix.

A new PfG should acknowledge that little progress can be made to reshape and realign the economy whilst the region remains disproportionally reliant on the public sector and on year-on-year increases in real terms public spending. As the public sector faces a declared £4bn cumulative decline and the agreement on the draft Budget reached by the Executive on 3 March does not fund this gap, the Executive must therefore plan for radical action to reduce the size of the public sector and accelerate private sector growth and influence.

---

[27] Professor R. Barnett 2009, *Independent Review of Economic Policy,* DETI and Invest NI, Belfast.
[28] Barnett, *op. cit.*

We make this recommendation notwithstanding the record of past performance whereby the Northern Ireland economy generally only converged towards the UK average during periods of rapidly growing public spending and by implication, therefore, the Northern Ireland private sector has not demonstrated much elasticity of response.

However, under the current circumstances, not only *should* things be different but *they have to be* and, given that the public expenditure constraints are both challenging and inevitable, the private sector and business leaders must accept that, just as they have been part of the problem, they are a key component of the solution.

Notwithstanding this, the private sector needs to be intelligently incentivised, not necessarily by a reduction in headline corporation tax (where every company receives a potential tax cut, whether they have earned it or not) and certainly not by a re-run of 1970s and 1980s grants and subsidies.

A new PfG, as it examines available research material, should include a radical review of Department numbers, Departmental activities and Departmental service delivery to identify significant opportunities for economies of scale, disposal of assets and externalisation of functions. The number of Assembly Departments could be reduced to, at most, six and the number of agencies could be readily externalised with no loss of service delivery. Programmes, currently undertaken at considerable cost inside the public sector, could be externalised to the private or voluntary sectors on the basis of performance reward.

The substantial delay to the reform of Education structures has already cost around £34m in potential saving and a further £20m in savings is lost every year a single education authority is delayed.

Similarly the opportunity to begin the reform of local government has been squandered and set back a further five years. Had the Reform of Local government started in 2011 as planned many of the fundamental reforms would have been completed by 2015 with savings accruing annually beyond that time. We should also acknowledge that Local government is an integral part of any new PfG and has a key role to play coordinating and facilitating collaboration around how services are delivered locally to best outcome.

The McKinsey Report[29] (tabled by DHSSPS during the consultation process) recommends, *inter alia*, a radical review of acute hospital provision and activities, and the PfG should address its recommendation. A PfG could also determine if assets and the revenue flow of organisations like NIHE and Translink could be leveraged to generate additional capital investment, while road-tolling could assist with funding additional infrastructure.

We believe the establishment of a Modernisation Committee – drawing on the expertise of the private sector and academia – be established to make recommendations on reducing Departmental numbers and externalising assets and service delivery. Such a committee could be based on the Special Group on Public Service Numbers and Expenditure Programmes[30] (*An Bord Snip Nua).*

[29] McKinsey February 2011, *Reshaping the System: Implications for Northern Ireland's Health and Social Care Services of the 2010 Spending Review.*

[30] Established by the Department of the Taoiseach on 27 November 2008, the Special Group on Public Service Numbers and Expenditure Programmes (also known as *An Bord Snip Nua*) was a four person group that included Colm McCarthy, an economist at UCD and Donal McNally, Second Secretary in the Department of Finance. *An Bord Snip Nua* was established to examine all programmes funded through public expenditure and determine whether financial resources were being optimally deployed to achieve priority policy objectives. The Group also identified options for savings in the context of the Government's fiscal objectives as set out in Budget 2009 and was charged with ensuring that public expenditure was being used to address relevant priority policy objectives.

The proposal from the coalition government to offer the Executive the potential to alter the rate of Corporation Tax should be a key objective in the PfG. However, we believe that tax varying powers may prove more rewarding and flexible than merely accepting the power to alter Corporation Tax alone as such powers could also designate Northern Ireland (or sections of the region) as Entrprise Zones, with sweeping powers to attract and incentivise both overseas and indigenous investment.

Turning to structure and content, we are attracted to the simplicity and directness of the PfG produced by the coalition on 31 May 2010[31] which featured some 399 commitments across 31 headings (Banking, Business, Civil Liberties, Consumer Protection… etc.), many of which might be described as 'recognition events' or outcomes that can be clearly imagined and where the delivery will be universally recognised and capable of evaluation. Statements such as "W*e will establish an independent NHS Board"; "We will publish details of every UK project that receives over £250,000 of EU funds"*; and "*We will ban the sale or alcohol below cost price"* are clear recognition events that can be monitored and challenged by interested parties.

Likewise, the Scottish Executive also produced their first PfG, *Working together for Scotland,* in 2001 and its successor document, *Delivering for Scotland*[32] in September 2010, in advance of the Scottish Budget. These included similar recognition events and in the case of *Delivering for Scotland*, included legislation that the Scottish Assembly has pledged to pass during the next year.

Ireland's newly elected Fine Gael / Labour coalition has demonstrated equal speed in negotiating and publishing a PfG [33] containing some particularly difficult decisions, particularly for Labour. The new coalition is committed to the previous administration's target of shrinking Ireland's budget deficit from nearly 12% of GDP currently, to below an EU limit of 3% by 2015. Other measures include:

- Finding €3bn savings in the Budget 2012, without decreasing social welfare rates.
- Maintain Ireland's corporate tax rate at 12.5%.
- Reduce the number of public sector employees by close to 10%, (cutting 18,000-21,000 jobs by 2014 and an additional 4,000 by 2015).
- Reverse the €1 cut in the minimum wage.
- Cut Ireland's lower rate of VAT to 12% from 13.5% for two years.
- Put water metres in every home.
- Limit the top rate of VAT to 23%.
- Consider various options on a property tax.
- Target up to €2bn in sales of non-strategic state assets.

---

[31] The Coalition May 2010, *op.cit.*
[32] Scottish Executive 2010, *op. cit.*
[33] The Irish Government March 2011. *Government for National Recovery 2011-2016*

We are particularly taken with the coalition commitment that "*...We will... within the first 100 days...*"[34]

- provide resources for an additional 15,000 places in training, work experience and educational opportunities for those who are out of work
- cut the 13.5% rate of VAT to 12% up to end 2013
- halve the lower 8.5% rate of PRSI up to end 2013 on jobs paying up to €356 per week
- reverse the cut in the minimum wage
- abolish the Travel Tax as part of a deal with airlines to restore lost routes
- implement a number of sectoral initiatives in areas that will create employment in the domestic economy
- initiate a long-term strategy to develop new markets in emerging economies
- secure additional resources for the national housing energy retrofitting plan, as part of plans to phase out subsidies in this area by 2014
- expand eligibility for the back to education allowance
- accelerate capital works that are 'shovel ready' and labour intensive including schools and secondary roads.

The speed and severity of the Irish coalition proposals, including the potential to externalise €2bn of State assets and implement water charging has sent a message to all sections of Irish society that the status quo is unsustainable; a message the Executive should study carefully.

[34] The Irish Government March 2011.,*op. cit*

We therefore believe that a new Northern Ireland PfG should include:

- A list of intended legislation for each of the next four years.
- Specific commitments related to economic, social, public service delivery, infrastructure and public sector reform.
- The total financial allocation, by Department, for each of the commitments.
- Recognition events, by Department, including target delivery dates that contribute to the specific commitment.
- Commitments to the reduction of Departments and the externalisation (i.e. commissioning) of Departmental service delivery.

We should acknowledge that successive Stormont, Direct Rule and Assembly administrations have tinkered with economic policy and wasted the opportunities to regenerate and realign the economy. We should also acknowledge that the PfG 2008-2011 has failed to achieve its objectives and that the region, in terms of relative wealth/productivity gap with the rest of the UK, has not advanced very far from where it was at the foundation of the state in 1921.

We cannot afford a further four years of tinkering with the economy or playing fast and loose with key public services. The next Executive must create a coherent and deliverable Programme for Government for Northern Ireland if it is to meet the expectations of the Good Friday Agreement and the hope of the rising generations of young people who believed that ,"under new management", things would be much, much better.

www.pwc.co.uk/ni

This publication has been prepared for general guidance on matters of interest only, and does not constitute professional advice. You should not act upon the information contained in this publication without obtaining specific professional advice. No representation or warranty (express or implied) is given as to the accuracy or completeness of the information contained in this publication, and, to the extent permitted by law, PricewaterhouseCoopers LLP, its members, employees and agents do not accept or assume any liability, responsibility or duty of care for any consequences of you or anyone else acting, or refraining to act, in reliance on the information contained in this publication or for any decision based on it.

© 2011 PricewaterhouseCoopers LLP. All rights reserved. In this document, "PwC" refers to PricewaterhouseCoopers LLP (a limited liability partnership in the United Kingdom), which is a member firm of PricewaterhouseCoopers International Limited, each member firm of which is a separate legal entity.