The (Dis)United Kingdom?

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Overview

• Regional economic and industrial disparities in the UK

• How have the nations of the UK traditionally been funded?

• Scottish Independence Referendum and How the UK is changing

• Why Wales, Scotland & NI support a Soft Brexit
The UK’s Major Economic Discrepancies

- **London** has the largest Gross Value Added (GVA) per head at £37,232 – 171% of the UK average

…while **Wales** had the lowest at £15,401 per head, just 71% of the UK average.

1. **101%** of UK average (Population of 53m)
2. **92.3%** (5.3m)
3. **75%** (1.8m)
4. **71%** (3.1m)

*This has an impact on taxes collected that pay for public services >>*
GDP per head: How do the UK regions compare with the Belgian regions?
GVA per head – a closer look at the data

- Breaking GVA per head down to wages and profits
- Wages (employee compensation per employee) more evenly distributed across regions than profits.
- Regional wage inequality has been decreasing...
- But distribution of profits across UK regions has become more unequal – rising inequality in rental incomes (especially in London)
Fiscal Transfers

- Differential economic performance and asymmetric shocks are reflected in fiscal transfers throughout the UK.

- System of fiscal equalisation between UK regions not explicit (as in some federal countries), but implicit and automatic due to centralisation of UK public finances.

- **Government Expenditure and Revenue Wales 2016** estimated that difference between total government expenditure for Wales and revenues raised in Wales was £14.7 billion by 2015 – around 24% of Welsh GDP.
Fiscal Transfers

- Only London, the South East and the East of England make a positive contribution to the UK public finances.

- However, these estimates measure expenditure for each region, as opposed to expenditure in each region. Much expenditure takes place in London for example, but for the benefit of other regions.
Migration

- Theory would also suggest labour movement as a stabilising factor between regions. But labour highly heterogeneous.

- Net migration between Wales and England very small.
  - However, there are large and illustrative differences by age group – not fiscally neutral.

- Large outflow of graduates and young professionals from Wales to large cities in England.
UK tax base heavily dependent on London & South East economy

Share of total government revenue raised in London & South East

Source: Office for National Statistics
Public investment in infrastructure highly concentrated in London

Elizabeth Line: Change in property values since 2009

Government directed spending on Research and Development unevenly spread

Government, university and charity spending on R&D (£ per person per year)

- London
- Scotland
- South East
- East of England
- South West
- Yorkshire and The Humber
- North East and North West
- Wales
- East Midlands
- Northern Ireland
- West Midlands
BBC as an example...
How Taxpayers’ Pounds are (traditionally) spent in the UK

- **Block Grant** (calculated by the “Barnett Formula”)
- **Grants to Municipalities** to fund local services

- **£28 B** (Taxes Collected and Pooled from across the UK)
- **£15B**
- **£11 B**
- **£600 B**
Financing the UK’s nations – traditionally one of the most centralised systems in the developed world

- **Wales, Scotland and Northern Ireland’s devolved governments are funded primarily by a Block Grant**
  - This Grant (“Welsh Block”, “Scottish Block” etc.) is calculated mainly by the controversial **Barnett Formula**

- System gives full flexibility to the regional governments on **how** to spend their allocation…
  - But the **total size** of their budget is set by Westminster:
Financing the UK’s nations – how does it work?

- **UK spending is NOT based on relative need of the 4 countries**
- The formula consists of each country’s prior year funding plus an uplift, termed a “consequential”
- The formula causes spending to automatically increase in Scotland, Wales and NI based on (a) their population, (b) and spending increases on comparable public services in England
  - The size of the budget in Wales, NI and Scotland is determined by spending decisions for England!
Financing the UK’s nations – the missing accountability link

- No link between devolved budgets and the amount of taxes raised in Wales, Scotland and Northern Ireland
- Devolved elections are fought on how to spend public money, not how it is raised
- No budgetary incentive to grow Welsh economy for Welsh Governments
The Barnett Formula was introduced for Scotland in 1978 and for Wales in 1980 on a temporary basis:

- Formula was never meant to last (and was later disowned by its ‘author’, Joel Barnett!)

- But it is straightforward to operate for the UK

- Was designed to avoid cabinet disputes over territorial funding for the Scotland, Wales and NI territorial offices

- BUT - At first glance, the devolved countries do receive higher funding per head than does England…

Why the old system survived for so long
The Celtic Spending Bonus

Identifiable public spending per person in **England** is currently £8,638 per year (2014-15, Treasury data)

But spending in:

- **Scotland** is 20% (£1,736) higher
- **Wales** is 15% (£1,266) higher
- **Northern Ireland** is 29% (£2,468) higher

But the operations of the formula are not quite as benign as first appears...
The reaction to Barnett Formula across the UK

• **Criticism** in **England** focuses on lower public spending relative to Scotland (no tuition fees, free personal care for the elderly, etc.)

• **Criticism** in **Wales** – concern that Wales is underfunded because of greater public spending needs

• Referendum issue in **Scotland**: **support** for **retaining** the formula (and higher spending levels) was key for the No campaign
Recent Scottish politics

INDEX OF DISSIMILARITY, SCOTLAND AND WALES
(COMPAARED TO ENGLAND), 1945–2015 GENERAL ELECTIONS
2014 Scottish Referendum

- Weekend before referendum:
  - Poll: Yes 51% No 49%
- Unionist parties agree additional powers to prevent “Yes” vote

Daily Record, September 16, 2014
Aftermath of Referendum

- **Smith Commission** established in Sep 2014 to generate a rapid cross-party agreement
  - Large public engagement: *Over 17,000 contributions received in first month!*

- Led to **Scotland Act 2016**
  - New powers over employment support, welfare
  - **Scottish Parliament gains control of virtually all Income Tax, 50% of VAT, many smaller taxes**
Progression of new powers transferred to Scotland

Devolved and Reserved Revenue in Scotland 2015-16

Devolved and Reserved Expenditure in Scotland 2015-16

Source: Government Expenditure and Revenue Scotland 2015-16
### New Devolved Taxes

<table>
<thead>
<tr>
<th>Tax</th>
<th>Welsh Revenue</th>
<th>Scottish Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>Council Tax</td>
<td>£2.1 billion</td>
<td>£1.3 billion</td>
</tr>
<tr>
<td>Business Rates</td>
<td>£1.9 billion</td>
<td>£850 million</td>
</tr>
<tr>
<td>Land and Buildings Transaction Tax</td>
<td>£400 million</td>
<td>£170 million</td>
</tr>
<tr>
<td>Landfill Tax</td>
<td>£150 million</td>
<td>£50 million</td>
</tr>
<tr>
<td>Welsh Income Tax (reduces each UK rate by 10p)</td>
<td>.</td>
<td>£1.9 billion</td>
</tr>
<tr>
<td>Scottish Income Tax (all earned income)</td>
<td>£11.2 billion</td>
<td>.</td>
</tr>
<tr>
<td>Air Passenger Duty</td>
<td>£275 million</td>
<td>.</td>
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<tr>
<td>Aggregates Levy</td>
<td>£50 million</td>
<td>.</td>
</tr>
<tr>
<td>50% of Value Added Tax (VAT) – assigned</td>
<td>£5 billion</td>
<td>.</td>
</tr>
</tbody>
</table>
How have Wales and Scotland’s settlement changed?

Brexit and the Economy - Challenges

• Significant budget questions for Wales

• Repatriation of competences over agriculture, environment and regional policy

• Differentiated regional impact of the Brexit deal

• Single Market, Customs Union, Trade questions
### Average receipts from major EU programmes per year, 2014-2020

<table>
<thead>
<tr>
<th></th>
<th>England</th>
<th>Northern Ireland</th>
<th>Scotland</th>
<th>Wales</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Common Agricultural Policy - total spending</strong></td>
<td>£2,184 m</td>
<td>£317 m</td>
<td>£614 m</td>
<td>£353 m</td>
</tr>
<tr>
<td><strong>CAP spending per capita</strong></td>
<td>£31</td>
<td>£145</td>
<td>£96</td>
<td>£96</td>
</tr>
<tr>
<td><strong>Structural funds total spending</strong></td>
<td>£735 m</td>
<td>£54 m</td>
<td>£95 m</td>
<td>£255 m</td>
</tr>
<tr>
<td><strong>Structural funds spending per capita</strong></td>
<td>£13</td>
<td>£30</td>
<td>£18</td>
<td>£83</td>
</tr>
</tbody>
</table>

Source: Centre for European Reform (CER) 2014
Soft Brexit interests in Wales, Scotland and NI

- Wales is a net beneficiary from EU budget (£245M/yr)
- Manufacturing Sector: Wales & Scotland far more dependent on the EU for its export markets
  - Over two-thirds of Welsh exports currently are to the EU, compared with less than half of exports from the UK as a whole.
- Hard Border / Peace Process concerns in NI
Brexit & Regional Industrial Differences

Public Services
Business Support Services
Real estate
Finance
Communication
Distribution, food, transport
Construction
Manufacturing
Agriculture, mining

Recreation
• **CAP Funding:** Wales has been allocated more than EUR2.2 BN between 2014-2020
  - More than 80% of farming income in Wales originates from EU funding.

• **Importance of export market:** Welsh food and drink exports to the EU worth £274.2 million in 2014, 90.7% of total exports. Only 9.3% went to non-EU countries.

• **Agriculture policy is a devolved competence**
  - Increasing policy divergence between Wales and Scotland on the one hand, and the UK on the other, on a wide range of agricultural issues.
GENERAL ELECTION 2017

England After 533 of 533 seats

<table>
<thead>
<tr>
<th>Party</th>
<th>Seats</th>
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<tbody>
<tr>
<td>CON</td>
<td>297</td>
</tr>
<tr>
<td>LAB</td>
<td>227</td>
</tr>
<tr>
<td>LD</td>
<td>8</td>
</tr>
<tr>
<td>GRN</td>
<td>1</td>
</tr>
<tr>
<td>UKIP</td>
<td>0</td>
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Change:
- CON: -22
- LAB: +21
- LD: +2
- GRN: +0
- UKIP: -1

Scotland After 59 of 59 seats

<table>
<thead>
<tr>
<th>Party</th>
<th>Seats</th>
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</thead>
<tbody>
<tr>
<td>SNP</td>
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<tr>
<td>CON</td>
<td>13</td>
</tr>
<tr>
<td>LAB</td>
<td>7</td>
</tr>
<tr>
<td>LD</td>
<td>4</td>
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</table>

Change:
- SNP: -21
- CON: +12
- LAB: +6
- LD: +3

Wales After 40 of 40 seats

<table>
<thead>
<tr>
<th>Party</th>
<th>Seats</th>
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</thead>
<tbody>
<tr>
<td>LAB</td>
<td>28</td>
</tr>
<tr>
<td>CON</td>
<td>8</td>
</tr>
<tr>
<td>PC</td>
<td>4</td>
</tr>
<tr>
<td>LD</td>
<td>0</td>
</tr>
</tbody>
</table>

Change:
- LAB: +3
- CON: -3
- PC: +1
- LD: -1

Northern Ireland After 18 of 18 seats

<table>
<thead>
<tr>
<th>Party</th>
<th>Seats</th>
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</thead>
<tbody>
<tr>
<td>DUP</td>
<td>10</td>
</tr>
<tr>
<td>SF</td>
<td>7</td>
</tr>
<tr>
<td>SDLP</td>
<td>0</td>
</tr>
<tr>
<td>UUP</td>
<td>0</td>
</tr>
<tr>
<td>OTH</td>
<td>1</td>
</tr>
</tbody>
</table>

Change:
- DUP: +2
- SF: +3
- SDLP: -3
- UUP: -2
- OTH: +0
Diolch Diweddd

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