

Written evidence submitted by the Institute for Government

Background

1. The Institute for Government is a non-partisan think tank, which aims to improve the effectiveness of government. We have been conducting research throughout the Covid-19 crisis on how well the Treasury and other departments have designed and implemented policies to support the economy. These included a report into the use of the furlough scheme¹ and several reports comparing the UK response to those deployed by other countries – including on labour market support,² stimulus policies³ and business support.⁴
2. We have focused our answers on the institutional and policy approaches taken by government, rather than the broader economic consequences of this crisis. Our contributions point out some serious value-for-money concerns. We recommend greater targeting of support at businesses and sectors in need, the publication of detailed policy analysis and reforms to emergency procurement processes in case of a future crisis. We also recommend changes to spending reviews and to the scrutiny of fiscal rules to make them more robust.

Questions

To what extent do Government measures protect viable jobs in the future and reduce the risk of long-term unemployment?

3. The government has two main means of preventing long-term unemployment: helping companies preserve existing jobs and encouraging the creation of new ones. It has, thus far, been more ambitious and successful at the former, although that is understandable considering there is still significant uncertainty about which sectors will create employment in future.⁵
4. The IfG's work on the Coronavirus Job Retention Scheme (CJRS) has suggested that the scheme helped protect viable jobs in the spring. Countries which implemented less generous wage subsidies, implemented them too slowly or did not implement them at all experienced sharp increases in unemployment.⁶ The UK scheme was a success in the spring and was designed and tapered such that cost to the taxpayer was not excessive. Iterations to the scheme, especially the possibility of part-furloughing employees from July, have helped preserve jobs. Part-furlough has allowed companies to retain support from the government while employees keep their skills

¹ Pope T, Dalton G and Tetlow G, 'The Coronavirus Job Retention Scheme', Institute for Government, 22 October 2020, <https://www.instituteforgovernment.org.uk/publications/coronavirus-job-retention-scheme>

² Tetlow G, Pope T and Dalton G, 'Coronavirus and unemployment: a five nation comparison', Institute for Government, 29 May 2020, <https://www.instituteforgovernment.org.uk/publications/coronavirus-unemployment-five-nation-comparison>.

³ Pope T and Dalton G, 'Stimulus policies after the coronavirus shutdown', Institute for Government, 7 July 2020, <https://www.instituteforgovernment.org.uk/explainers/stimulus-policies-after-coronavirus-shutdown>

⁴ Tetlow G and Dalton G, 'Support for business during the coronavirus crisis', Institute for Government, 6 October 2020, <https://www.instituteforgovernment.org.uk/publications/support-business-coronavirus>.

⁵ Office for Budget Responsibility, 'Economic and fiscal outlook – November 2020', 25 November 2020, <https://obr.uk/efo/economic-and-fiscal-outlook-november-2020/>.

⁶ Tetlow G, Pope T and Dalton G, 'Coronavirus and unemployment: a five nation comparison', Institute for Government, 29 May 2020, <https://www.instituteforgovernment.org.uk/publications/coronavirus-unemployment-five-nation-comparison>.

intact by returning to work part-time. Nearly a third of employees on the scheme are part-furloughed, according to the most recent data.⁷

5. However, the government's delay in deciding to extend the CJRS in the autumn caused unnecessary uncertainty for businesses and may have resulted in layoffs which would not otherwise have occurred. The Treasury should make more of an effort to communicate policy changes earlier and, if possible, set out under what conditions support will be granted in case of future tightening or extension of public health restrictions.
6. The lack of use of the CJRS during the second and third lockdowns⁸ is to the government's credit. Better communication about what work could and could not continue during the second English lockdown meant that far more companies were able to stay open and keep workers employed. Furlough rates in most sectors did not significantly increase in November according to ONS business survey data, and even in sectors where furloughing increased during the second and third lockdowns – like arts and recreation and food and accommodation – it did not return to April levels.⁹ Since this has not been accompanied by any substantial fall in the overall number of jobs, this suggests that many workers furloughed in the spring have been able to continue working during the second and third lockdown.
7. Some of the government's job creation initiatives are encouraging so far – especially the creation of the Kickstart and Restart schemes. But IfG research shows that more ambition is needed. In particular, support needs to be better extended to those ineligible for Universal Credit (for example, because their savings are too high or their partner earns too much), who are currently unable to access a DWP work coach or the resources work coaches can use.
8. Better co-ordination between the departments responsible for helping people into work – including the Department for Work and Pensions (DWP), the Department for Business, Energy and Industrial Strategy (BEIS), the Treasury and others – will also be crucial in creating a more joined-up approach to job creation. There should also be more use of local expertise in helping people into work. Councils and Jobcentres know – or should know – their local labour markets well and are able to act as convenors to bring together employers, Jobcentres, the National Careers Service, Local Enterprise Partnerships and local further and higher education providers.

To what extent are Government measures value for money for the taxpayer?

9. The government was right to act quickly and disregard some value for money concerns in the spring in the interests of providing support quickly to people and businesses. However, while generous and bold support was to be welcomed, there are several examples of policies that have been poor value for money because they are poorly targeted, subject to fraud or both.
10. The self-employment income support scheme (SEISS) allowed recipients to keep trading and receive a grant even if they were not badly affected by Covid. Analysis has shown that the

⁷ According to data from Office for National Statistics, 'Business insights and impact on the UK economy', 28 January 2021, <https://www.ons.gov.uk/economy/economicoutputandproductivity/output/datasets/businessinsightsandimpactontheukeconomy>.

⁸ For example, less than a third of those who had come off the scheme after the first lockdown were re-furloughed during the second lockdown.

⁹ Pope T, 'Government deserves credit for reducing the economic costs of coronavirus lockdown', Institute for Government, 17 December 2020, <https://www.instituteforgovernment.org.uk/blog/government-deserves-credit-reducing-economic-costs-coronavirus-lockdown>.

money is poorly targeted at those who are adversely affected by Covid.¹⁰ It is set to cost over £20bn this year, more than one-third of the cost of the CJRS.

11. The CJRS was the right policy to pursue and has had a significant impact on reducing unemployment and preserving viable jobs, as mentioned above. In that way, it has presented good value for money. The terms on which the scheme was set out, in particular the decision only to subsidise wages for hours workers were not able to work, ensured good value for money as it incentivised employers to stop using the scheme when work returned. As a result, the number of workers on the scheme (and therefore its cost to the taxpayer) reduced by around 75% between April and October.¹¹
12. However, the scheme itself is not as well targeted as it could be because it provides equally generous support to businesses badly affected by coronavirus and those not adversely affected. This means that money is wasted supporting unviable jobs in otherwise economically healthy sectors, including sectors where employment is expanding. The IfG has proposed a sector-by-sector approach to improve the targeting at long-term viable jobs.¹²
13. The Bounce Back loans scheme, which provides a 100% guarantee to loans offered to small businesses, is forecast to cost the government £26bn. Acquiring a loan is possible with minimal checks. This has achieved one goal of the policy – getting money quickly to businesses in need – but at a very high cost and with a very high anticipated default rate.
14. The scheme has undoubtedly helped some businesses with liquidity constraints to survive through 2020. But 35-60% of claims are expected not to be paid back either because the claims were fraudulent or because the recipient businesses are expected to become insolvent or be so weak they will never be able to pay it back.¹³ In other words, tens of billions of pounds of public money are thought to have been paid to fraudsters or to the weakest subset of firms.¹⁴ The loans face the additional downside of weighing companies down with debt in future, potentially restricting their ability to invest and to access other capital.¹⁵
15. The UK is unusual internationally in making much of its coronavirus business support available to all, rather than restricting only to those that have been substantially adversely affected by the pandemic; the exception to this is government-guaranteed loans, which are only available to those businesses that have been negatively affected by Covid. Most other countries we have studied have only offered grants to businesses with significant drops in revenue (France, Germany, Japan, Norway) or put in place loss carry-back tax policies that specifically compensate previously profitable businesses that incurred losses in this crisis (Germany, Japan, Norway, New

¹⁰ Brewer M, Cominetti N, Henahan K, McCurdy C, Sehmi R and Slaughter H, 'Jobs, Jobs, Jobs', Resolution Foundation, 27 October 2020, <https://www.resolutionfoundation.org/publications/jobs-jobs-jobs/>.

¹¹ According to data from Office for National Statistics, 'Business insights and impact on the UK economy', 17 December 2020, <https://www.ons.gov.uk/economy/economicoutputandproductivity/output/datasets/businessinsightsandimpactontheukeconomy>.

¹² Pope T, Dalton G and Tetlow G, 'The Coronavirus Job Retention Scheme', Institute for Government, 22 October 2020, <https://www.instituteforgovernment.org.uk/publications/coronavirus-job-retention-scheme>.

¹³ Estimates from the Department for Business, Energy and Industrial Strategy, 'BEIS annual report and accounts 2019 to 2020', 30 September 2020, <https://www.gov.uk/government/publications/beis-annual-report-and-accounts-2019-to-2020>.

¹⁴ Durrant T et al, 'Whitehall Monitor 2021', 28 January 2021, <https://www.instituteforgovernment.org.uk/publications/whitehall-monitor-2021>.

¹⁵ Wilkes G, 'Bailout for business after coronavirus', Institute for Government, 29 April 2020, <https://www.instituteforgovernment.org.uk/publications/bailout-business-after-coronavirus>.

Zealand).¹⁶ Among nine countries that we studied, the UK was the only one to provide support to the self-employed regardless of whether or not they had been affected by the pandemic.¹⁷ This means that the UK has been unusual in giving money even to self-employed people who have done well or averagely out of the crisis.

16. This approach should be refined by the Treasury, to stop further money going to firms who are not in need or have even profited from the crisis. It should not be up to individual firms like Tesco's and Sainsbury's to give back money granted in the business rates holiday, for instance, but up to government to set the right rules.¹⁸ There should be more iteration in the schemes still available – and any support provided in future – to ensure that business support and support for the self-employed is directed towards those that have suffered the most from this crisis. While the lack of targeting was understandable at the outset of the crisis, when the priority was to distribute money quickly, it is less excusable ten months on.

How effective is the Government support to businesses and individuals across different regions and sectors? Does the effectiveness of the Government support vary across different regions?

17. The government's support to businesses has varied in effectiveness by sector because the challenges faced by sectors vary significantly. Because the CJRS is available to all businesses, regardless of how they have been affected by Covid, in those sectors where output has returned to or near pre-crisis levels (such as retail, financial services or real estate), the impact of furlough is to subsidise the weakest firms in the market who have not returned to full functionality. In mid-September, we estimated that these less impacted sectors accounted for around half of the 2.5m people still furloughed at that point.
18. The other half were furloughed in sectors like hospitality, arts and recreation, and administrative and support services which were still significantly impacted by restrictions. In these sectors, CJRS spending is likely to have been more effective, in the sense of paying the wages of workers who continued to be prevented from working due to restrictions or large Covid-related reductions in demand.

What improvements can be made to institutions to ensure that responses to crises like these are more robust in the future and policy makers have the data they need? What further analysis should the Government do and make transparent?

19. Government has adapted in response to this crisis. Some institutional changes have been very welcome. For example, the Business Impact of Covid-19 Survey created by the ONS has been able to provide rapid data on how businesses have fared in this crisis and adapted well to demands from government and other stakeholders for new information. This survey should be

¹⁶ Tetlow G and Dalton G, 'Support for business during the coronavirus crisis', Institute for Government, 6 October 2020, <https://www.instituteforgovernment.org.uk/publications/support-business-coronavirus>.

¹⁷ Pope T and Dalton G, 'Coronavirus: how have different countries supported workers through the crisis?', Institute for Government, 5 June 2020, <https://www.instituteforgovernment.org.uk/coronavirus-support-workers-comparison>.

¹⁸ Tetlow G, 'Supermarket cashback highlights need for Treasury to review its Covid rescue offer', Institute for Government, 10 December 2020, <https://www.instituteforgovernment.org.uk/blog/supermarket-cashback-treasury-covid-rescue>.

continued beyond the crisis phase of this pandemic as a vital information source for government and policymakers.

20. This crisis has also reflected well on the ability of some parts of government to make decisions and deal with change at short notice. For instance, the Treasury's ability to rapidly roll out the CJRS and DWP's ability to cope with a flood of new Universal Credit applicants are to be applauded.¹⁹ Again, government should try to preserve this spirit of rapid response and ambition to pursue rapid change in the civil service and in policy beyond the pandemic.
21. On the other hand, the approach taken to procurement in this crisis has been poor and lacked transparency.²⁰ As the National Audit Office (NAO) has laid out, normal procedure on procurement was often bypassed even in the later stages of the spring without a full justification for why normal processes could not be followed.^{21,22} Reforms to emergency procurement practices to safeguard against similar problems in future and make sure that procurement is as open and fair as possible, even when under time pressure, should be encouraged.
22. The government could also do more to publish accurate and timely information on how contracts were awarded, so that bodies without the access to internal government information that the NAO has can also scrutinise value for money.
23. The Treasury has been urged to publish a cost-benefit analysis of different public health restrictions. However, such an exercise would be almost impossible to perform because many of the necessary components of the calculation are unknown and it would involve some huge leaps of judgement on how to value different outcomes. It would, therefore, risk incorrectly framing as a scientific calculation what is inevitably a political judgement on the appropriate level of restrictions.²³ Nonetheless, the government should be encouraged to provide a clearer explanation of how economic considerations are factored into decisions and should be encouraged to carry out and publish more smaller pieces of analysis. In particular, it should analyse the impact of specific policy changes on the spread of the disease and on current economic activity – such as the 10pm curfew or the decision to keep gyms open – and use this to inform future policymaking. It should not be afraid of publishing studies looking at both the economic and epidemiological consequences of policy side-by-side – for example, in evaluating the Eat Out to Help Out scheme. It is always welcome for government to learn from its own failures and successes.

What are the consequences of high national debt? What should the new fiscal rules be?

24. While some (most famously Carmen Reinhart and Kenneth Rogoff²⁴) have suggested that there is a threshold level of external government debt above which economic growth rates decline,

¹⁹ Nickson S, A Thomas and E Mullins-Burgess, 'Decision-making in a crisis', 1 September 2020, <https://www.instituteforgovernment.org.uk/publications/decision-making-crisis-coronavirus>.

²⁰ Durrant T et al, 'Whitehall Monitor 2021', 28 January 2021, <https://www.instituteforgovernment.org.uk/publications/whitehall-monitor-2021>.

²¹ National Audit Office, 'Investigation into government procurement during the COVID-19 pandemic', 26 November 2020, <https://www.nao.org.uk/report/government-procurement-during-the-covid-19-pandemic/>.

²² Sasse T, 'The government must clean up its act on coronavirus contracts', Institute for Government, 20 November 2020, <https://www.instituteforgovernment.org.uk/blog/government-must-clean-its-act-coronavirus-contracts>.

²³ Wilkes G, 'The doubtful case for an impossible Covid-19 cost-benefit analysis', Institute for Government, 27 November 2020, <https://www.instituteforgovernment.org.uk/blog/doubtful-case-impossible-covid-cost-benefit-analysis>.

these conclusions are contested²⁵. More recent work has emphasised the importance of how any government borrowing, which increases public debt, is used – for example, the latest Fiscal Monitor from the International Monetary Fund encouraged governments to increase public investment in order to boost economic growth during the recovery from the coronavirus pandemic.²⁶

25. However, higher levels of government debt do increase the exposure of the public finances to changes in government borrowing costs and reduce scope for using fiscal policy to cushion future economic shocks. With monetary policy at or close to its limits, fiscal policy is likely to need to play a greater role in economic stabilisation over the next few years than it has done in some previous downturns, when monetary policymakers were able to have a greater impact by cutting interest rates.
26. While there is no clear threshold above which UK public debt becomes unsustainable, it is unsustainable for the UK government to keep increasing public debt relative to GDP every year. The latest official forecasts from the Office for Budget Responsibility (OBR) suggest that this is what would happen unless the government cuts back some areas of public spending or announces new tax rises.²⁷
27. Past fiscal rules – which have targeted public sector net debt and one or other of public sector net borrowing and the current budget balance – have had flaws and encouraged or enabled some perverse behaviour. For example, since public sector net debt captures only the value of liquid but not illiquid public sector assets, previous chancellors have timed the sale of illiquid assets (such as the student loan book) in order to game the rules, even though such actions may not have strengthened (and sometimes actually weakened) the public sector's underlying asset position. Similarly, forward-looking borrowing targets have allowed successive chancellors to pencil in future spending cuts to meet those targets but then not been delivered.
28. Notwithstanding those problems, fiscal rules impose useful discipline on governments – avoiding some of the short-termism and pro-cyclicality that characterised UK fiscal policy before the advent of such rules. They help to ensure that ministers face up to the trade-offs needed to run sustainable public finances.
29. There are some improvements that could be made to previous incarnations of the fiscal rules – such as targeting a wider measure of public sector net worth.²⁸ However, no fiscal rules are infallible; all will have loopholes than can be exploited by the government if so desired. The rules must, therefore, be supplemented by rigorous independent scrutiny of the government's plans. The OBR has greatly increased the transparency of the public finances and fiscal plans in the UK. However, its remit limits it merely to judging whether the government has or has not met the letter of any fiscal rules. The OBR's analysis therefore needs to be used by others – including the

²⁴ Reinhart, C M and Rogoff, K S, 2010, 'Growth in a Time of Debt', *American Economic Review*, 100 (2); Reinhart, C M and Rogoff, K S, 2012, 'Public Debt Overhangs: Advanced-Economy Episodes since 1800', *Journal of Economic Perspectives*, 26 (3)

²⁵ Égert, Balázs, 2015, 'The 90% public debt threshold: the rise and fall of a stylized fact', *Applied Economics*, 47 (34–35)

²⁶ International Monetary Fund, 'Fiscal Monitor: Policies for the Recovery', October 2020, <https://www.imf.org/en/Publications/FM/Issues/2020/09/30/october-2020-fiscal-monitor>.

²⁷ Office for Budget Responsibility, 'Economic and fiscal outlook – November 2020', 25 November 2020, <https://obr.uk/efo/economic-and-fiscal-outlook-november-2020/> and Office for Budget Responsibility, 'Fiscal Sustainability Report', 14 July 2020, <https://obr.uk/fsr/fiscal-sustainability-report-july-2020/>.

²⁸ Hughes R, Pacitti C, Leslie J and Smith J, 'Totally (Net) Worth It', Resolution Foundation, 29 October 2019, <https://www.resolutionfoundation.org/publications/totally-net-worth-it/>

Treasury Select Committee – who can challenge the government on its adherence to the spirit as well as the letter of the rules.

The Spending Review was originally due in the Autumn 2019 but has now been postponed for more than a year. How robust is it in times of crisis?

30. In both 2019 and 2020, the government postponed the spending review and instead provided departments with a one-year settlement. In both instances, it was the correct decision.²⁹ A spending review is an important process to provide certainty to departments to allow them to plan. However, it is only possible to commit to long-term settlements for all departments when the government can set an overall spending ‘envelope’ with confidence. Long-term planning by departments is also only possible when the demands on public services can be predicted. In both 2019 and 2020, uncertainty surrounding the public finances related to Brexit and coronavirus meant an overall envelope could not be set with confidence and new demands on public services in the aftermath of the coronavirus pandemic have not yet become clear.
31. Spending reviews still serve a valuable role, and two years in which a multi-year spending review has not been possible do not change this. What these years have shown, however, is that it will not always be appropriate to hold a multi-year spending review or to stick rigidly to spending review plans in times of crisis.
32. There are ways in which the spending review process in non-crisis years could be made more robust and more effective.³⁰ Discussions between departments and the Treasury should focus on outcomes and what can be delivered as well as the level of the budget – they should be more than cost-containing exercises. A spending review process is also more effective when the spending envelope is set before departments are given their settlements, to help trade off different priorities across the whole of government. But in the past few years this approach has largely been abandoned. Pre-determined settlements for the NHS, schools and defence mean that budgets will already have been set for more than 60% of departmental day-to-day spending before the process begins.

What impact will a second lockdown have on the economy? How should the Government best support the economy if intermittent lockdowns become a feature over the next year?

33. The second and third lockdowns had a significant impact on the economy, but not on the same scale as the first lockdown – after both the government and businesses had learnt from the first lockdown about how to ensure that more activity could continue while still reducing social contact. An estimated 4.5m workers were furloughed at the start of the third lockdown; this is more than during the second lockdown but still well below the estimated 10m workers furloughed in April 2020.
34. Some sectors, like construction, saw only negligible increases furlough rates during the second or third lockdowns, despite nearly 50% of construction workers being furloughed in the spring. However, the sectors that were still heavily impacted by the second and third lockdowns – such

²⁹ T. Pope, ‘This is not the time for a three year spending review’, Institute for Government, 28 July 2020, <https://www.instituteforgovernment.org.uk/blog/multi-year-spending-review>

³⁰ M. Wheatley, B. Maddox and T. Kidney Bishop, ‘The 2019 Spending Review: how to run it well’, Institute for Government, 13 September 2018, <https://www.instituteforgovernment.org.uk/publications/2019-spending-review>

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as hospitality – did experience a fall in activity and rise in furloughing. The second and third lockdowns therefore had very distinct sectoral effects, with the additional furloughed workers predominantly in three sectors – retail, hospitality, and arts and recreation. It would therefore be logical for the government to take a sectoral approach to supporting the economy in case of future intermittent lockdowns.

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