Ulster Bank

North set to announce £20bn ‘waste management’ strategy

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The inevitability of fiscal austerity for Northern Ireland was outlined in this column last week. This was quickly followed by a sombre Budget which, as expected, failed to outline the precise scale of the fiscal pain that lies in store. Nevertheless, Alistair Darling, who has gained somewhat of a reputation for being one of those rare individuals in Government who tells it as it is, confirmed that the forthcoming public expenditure cuts will be *“deeper and tougher”* than those introduced by Margaret Thatcher during the 1980s.

The north escaped the public expenditure axe during the 1980s and its public sector remains right at the back of the current recession ‘roller coaster’. Nevertheless, Northern Ireland’s public sector has already heard the screams of horror from the private sector carriages at the front of the train as it too braces itself for its biggest drop in public expenditure on record.

According to the highly respected Institute of Fiscal Studies (IFS), the UK, and by extension Northern Ireland, is set to experience “two parliaments of pain”. At the same time, the executive will soon be preparing its programme for government for the three years from 2011 with the economy expected to remain the number one priority. As a result, the executive is now in the unenviable position of having to devise a hybrid strategy of simultaneously delivering the seemingly contradictory goals of fiscal austerity and promoting long-term economic prosperity.

In many ways, addressing these twin goals could be viewed as a £20bn ‘waste management’ strategy. As such, the executive could do well to adopt the ‘Reduce, Reuse and Recycle’ motto that we have all become familiar with. This has been successful in changing a culture of wasteful behaviour that was evident in the north for decades. First, the trigger for change was the recognition of the waste and cost that was being incurred. Second, this information was communicated to consumers through positive messaging and the design of incentives to encourage positive behaviours. Third, it only came to a head when it was recognised that current behaviour and levels of consumption were unsustainable. Equally, the UK’s and Northern Ireland’s consumption of public expenditure has been proven to be unsustainable and the degree of waste and efficiency tolerated over the last decade is now being recognised. Yet at the same time, demand for increased and improved public sector service provision continues to grow unabated. Within this context the “Do Nothing option” is not an option.

Recently the Stormont executive has pushed through £350m of public expenditure cuts for the financial year beginning in April. These will be followed by around £700m in the 3 years from 2011/12 to 2013/14. To put this into perspective, this would be broadly equivalent to shutting the Department of Agriculture for 3 years or cutting the public sector pay bill by one third for those departments outside of health & education over the same time period. Moreover, the public expenditure squeeze will continue into the second parliament of pain. Given that public sector wages and salaries account for 50% of the executive’s budget and the consensus economic opinion is that capital expenditure (*infrastructure investment*) should be protected at all costs, it is inconceivable that current levels of public sector pay and employment can be protected. To date, the public sector has shown great flexibility in employment practices, it now needs to extend this to pay. After all, if Northern Ireland is to apply best practice in delivering fiscal austerity, public sector pay / pension cuts will be a key feature of this strategy.

Against the backdrop of more than 32,000 joining the unemployment register, widespread pay cuts, the widening public sector wage premium relative to the private sector and the UK public finances in the worst state since the Second World War, public sector unions in the north now find themselves in the weakest negotiating position imaginable. Conversely, the Executive could not have a stronger hand to exert meaningful reform with public sector pay and conditions.

In this new era, the Executive needs to ensure that pay rises are linked to productivity gains. For many in the public sector; productivity, flexibility and value for money are not appreciated yet in the parallel universe that is the private sector they are the difference between bankruptcy and survival.

Reducing the number of departments and public sector bodies is a given. Alongside the pay correction, there is a need to reduce the NICS headcount. The CBI's response to the Executive's Spending Plans 2010/11 highlighted reducing the size of the civil service by at least 10% over the next 3 years. However, the civil service could comfortably lower its headcount by 15-20%. This would release funds into either pro-economic development areas or frontline public services. Reducing the number of "junior" NICS grades from 7/8 to 4/5 would make for a more effective and less hierarchical structure.

Northern Ireland businesses are encouraged to apply best practice, to be more innovative and entrepreneurial. The executive needs to apply these same steps in delivering its £20bn 'waste management' strategy. Over the last twenty years or so not upsetting the apple cart appears to have been the modus operandi for economic development. With the public finance cart overturned, it is now time to do so. And Northern Ireland should look at policies that have been applied elsewhere and reuse them here.

So what form of fiscal austerity could NI adopt? Looking at the Greek response, its austerity packages have included unprecedented public sector pay cuts and rises in indirect taxes such as VAT. Alongside these standard responses there have been more unorthodox suggestions. Two of Germany's rightwing politicians suggested that Greece should consider selling off some of its islands and historic buildings to repay its public sector debt. Other ideas have included raising finance through an 'Acropolis bond' backed by the future stream of tourist revenues. I'm not advocating a 'for sale' sign on Rathlin Island or for the Executive to create a Giant's Causeway tourism bond. That said, the principle of selling off assets and exploring all routes to funding economic development should be explored.

On the recycle front, the Executive could look into auctioning off some of its public sector assets (privatisations) and adopting a '*cash for clunkers*' or '*swappage*' style of economic development. That is, trading in blocks of public expenditure that are inefficient and have systematically failed to promote economic development for ones that do. It should be remembered that despite Northern Ireland's consistently higher levels of public expenditure per head, relative to any other UK region, there has been no meaningful improvement in relative economic prosperity.

Undoubtedly a lower corporation tax would represent one such radical departure from current policy and if delivered would be unambiguously positive for the local economy. The benefits of a lower corporation tax are obvious; however, what is most significant within the proposal is the concept of devolving aspects of fiscal powers to NI and offsetting public expenditure accordingly. In effect, this is one example of better aligning public expenditure with the goals of economic development. NI should look at trading in or auctioning off other aspects of public expenditure for new or improved policy flexibility. Public expenditure sacrifice for policy gain should be a key theme.

This principle could be extended to developing new sources of revenue. If you introduced a public sector pension levy in the north as seen in the Republic, could Northern Ireland keep the revenue and invest (recycle) that into an infrastructure fund? This adopts the principle of the bank levy in the UK which has been used to finance a business support package fund in the UK. Northern Ireland should look into adapting similar 'Robin Hood' policies to redistribute or recycle its wealth from the public sector to the private sector.

Social security benefits are set at a national level, whereas pay rates in Northern Ireland are one of the lowest of any UK region - so this is a huge disincentive to work. If we introduced regional social security payments would the north be able to keep all or part of the savings and recycle to pay for schemes to get the long-term unemployed / inactive back to work or fund a Social Skills & Infrastructure fund?

These need to be openly debated. Regional public sector pay would be an extremely powerful economic development tool for the Executive and is also attractive from a public expenditure viewpoint, particularly if Northern Ireland could retain the savings to be invested elsewhere. Public sector pay is the one lever the north could use to better effect. Up until now it has pulled it in the wrong direction.

Fiscal reform has surged to the top of the economic agenda both at home and abroad. It is vital for Northern Ireland's future economic development that the Executive, like other administrations, also embraces fiscal reform to deliver its number one priority. We need to wake up to waste; and quickly!

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