HMT 2013 Spending Review: transport number crunch

Executive Summary

The 2013 Spending Round (commonly referred to as the 'Spending Review') announced a step change in infrastructure investment[1], backed by an impressive array of specific commitments[2]. But although the key transport capital budgets have emerged as obvious winners, the picture is less clear when it comes to some of Department for Transport's (DfT) smaller grants. At the same time, the unexpected decision to pool a substantial proportion of local transport capital funding into the Single Local Growth Fund (SLGF) makes the long term outcome uncertain. A clearer picture is unlikely to emerge until the DfT clarifies its detailed spending plans for 2015 onwards and the results of the first SLGF competition emerge in the second half of 2014. The key points from the Spending Round are summarised below.

Treasury big picture:

- The June Spending Round did not entail any net change in overall government spending relative to the March budget.
- In reality, the annual year-on-year growth in total government capital spending between 2014-15 and 2017-18 will most likely fall below the rate of inflation.
- The Spending Round did include some new capital funding commitments beyond 2018, with HS2 and the Highways Agency emerging as the big winners.
- Although overall capital expenditure will be higher in 2014/15 than originally set out in the 2010 Comprehensive Spending Review (CSR), this will be at the expense of resource budgets, which will be 8.5% below original plans. This is of particular significance to local government funding, which has been the main source of savings.

DfT budget:

- In 2015-16, the DfT's budget will be 4.5% lower than in 2014-15 (as set out in the March 2013 budget).
- Although DfT capital funding will increase by 6.7% (from £8.9 to £9.5 billion), its resource budget will go from £4.4 to £3.2 billion. The largest chunk of the saving will come from Transport for London's (TfL) resource grant and assumed efficiency savings in Network Rail spending and DfT's rolling stock procurement.

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[1] Amongst other things, the Chancellor promised "*the largest programme of investment in our roads in half a century*" and "*the largest rail investment since the Victorian era*".
[2] Stated in *Investing in Britain's Future*, the sister report to the 2013 Spending Round

- Our previous analysis of the 2010 CSR and subsequent budgetary announcements up to Autumn 2012 provides additional background information.

Local transport:

- There will be a significant boost to key local transport capital grants[3] in 2015-16:
  - +28% in real terms, relative to the 2014-15 budget
  - +16% in real terms relative to Labour's 2010-11 budget
- However, the unexpected decision to route a large proportion of local transport grants into Local Enterprise Partnerships (LEPs) via competitive growth deals makes it difficult to anticipate what proportion of this money will end up funding transport schemes in PTE areas.
- The Spending Round said nothing about what will become of smaller competitive grants such as the Pinchpoint Fund, the Green Bus Fund, the Cycle Ambition Grant or the DfT's contribution to the Regional Growth Fund. However, even if these were to be scrapped altogether, local transport capital funding would still increase by around 15% (in real terms) between 2014-15 and 2015-16.
- On the revenue side, the current rate of Bus Service Operators Grant (BSOG) has been protected until 2015-16 and we also know that the DfT will manage a considerable Local Sustainable Transport Fund (LSTF) resource grant in 2015-16.

[3] The % change figures are calculated for Integrated Transport Block, major schemes and highways maintenance grants only.

Introduction

Investing in Britain's future, the HM Treasury paper which followed the 2013 Spending Round, made quite an impression by suggesting that Britain is about to see a step change in infrastructure investment. One table, in particular, grabbed people's imagination. Titled *Government long-term spending plans,* it suggested that public spending on the road, rail and local transport networks would more than double between 2015 and 2020[4]. At the same time, it showed Transport for London's capital grant increasing below the rate of inflation, which suggested the government had finally come to grips with the transport funding gap between London and the rest of the country. As part of the Spending Round announcements, the government had also committed to the Bus Operators Service Grant at least in the short term and to extend the Local Sustainable Transport Fund into 2015/16.

Set against a background of sustained fiscal retrenchment, when some government departments are set to experience cuts of 10% in 2015/16, transport was seemingly one of the biggest winners from the Spending Round. Closer inspection, however, shows that there is still a risk of cuts to some of DfT's smaller grants. Taken together with changes in grant allocation methods this makes the overall outcome for local transport spending still uncertain.

This paper takes a closer look at the overall funding envelope for the UK government and the Department for Transport and how this has evolved, at a relatively high level, since the 2010 Comprehensive Spending Review (more detail about budgetary decisions up to the 2012 Autumn Statement can be found in a ***pteg***'s February 2013 number crunch). We then go on to discuss the balance between resource/revenue and capital budgets and the specific challenges facing local transport over the next couple of years as a result of the Spending Round.

Budget big picture

It is useful to start by understanding how the government's overall budget has evolved since the 2010 CSR, how it is set to change over the next four years and what impact the June Spending Round announcements have had. Table one shows annual Total Managed Expenditure (TME)[5] taken directly from the 2010 CSR, the 2013 Budget and the 2013 Spending Round.

These figures suggest that the June 2013 Spending Round (SR) and the March 2013 budget are based on the same assumptions about total government expenditure, both in terms of TME and capital spending. Hence, the SR does not entail any net change in overall government spending.

Moreover, the SR's overall budget (TME) for 2013-14 and 2014-15 is lower than originally set out in the 2010 CSR, although capital expenditure is in fact higher. Taken together with the fact that Resource Annually Managed Expenditure (AME)[6] has been significantly higher than forecast then it becomes clear that Departmental Expenditure Limits (DEL)[7] have, in practice, been cut even more severely than

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[4] In the case of local transport, it implies that the total funding available for local major schemes between

[5] Made up of total current expenditure and total capital expenditure, including an estimate of depreciation

[6] This includes demand-dependent or inflation-indexed expenditure such as welfare payments and pensions.

[7]

suggested at the 2010 CSR. Inspection of HMT tables shows that Resource DEL in 2014/15 will be 8.5% lower than originally budgeted in the 2010 CSR. This is particularly significant for local transport funding, which has been one of the most important sources of savings.

Finally, and despite the tone of *Investing in Britain's Future*, the annual year-on-year growth in total government infrastructure investment between 2014-15 and 2017-18 will likely fall below the rate of inflation.

Table one: Total managed expenditure (£bn p.a.)

	2013-14	**2014-15**	**2015-16**	**2016-17**	**2017-18**
TME – capital and revenue					
CSR 2010	724.2	739.8	-	-	-
Budget 2013	720.0	730.4	744.7	754.9	765.1
SR 2013	720.0	730.3	744.7	754.9	765.1
Annual % increase	-	*1.4%*	*2.0%*	*1.4%*	*1.4%*
Capital only					
CSR 2010	45.6	47.1	-	-	-
Budget 2013	47.2	50.4	50.4	51.3	52.1
SR 2013	47.1	50.4	50.4	51.3	52.1
Annual % increase	-	*7%*	*0%*	*1.8%*	*1.6%*

Altogether, this high level analysis suggests that the plans set out in *Investing in Britain's Future* do not imply any new real-terms funding increase for infrastructure or otherwise, at least until 2018. What they do show is the government's commitment to funding certain types of infrastructure (in particular, strategic transport schemes). Given that overall capital spending is set to fall in real terms from 2015/16, then it is clear that some of the capital programmes announced (HS2, roads, major schemes) will reduce the amount of funding available in other areas. We know that some of the required savings will come from TfL's funding and assumed efficiency savings in Network Rail's capital spending and DfT's rolling stock procurement. However, there are a number of smaller transport programmes which are as yet un-accounted for.

At the same time, resource budgets will continue to suffer severe year on year cuts far exceeding any small increases in overall capital spending.

Overall, it's unclear what this will all mean for local transport spending, which depends on some of DfT's smaller grants and Department for Communities and Local Government (DCLG) funding as well as DfT's larger capital programmes. We delve deeper into these issues in subsequent sections.

Departmental budgets – transport versus the rest of the world

Although the Spending Round announcement made no changes to the overall level of government spending for the next four years, it did provide new insights into government priorities from 2015-16. The initial reaction from officials suggested that the DfT had made a particularly successful case to Treasury and, as a result, its budget was set to increase.

Table two compares the planned change in departmental budgets between 2014-15 and 2015-16 for the DfT, Department for Business, Innovation and Skills (BIS) and DCLG, three of the largest departments whose budgets were not protected. Taking the Spending Round 2014-15 figures as the baseline, it does show an increase in the DfT's budget of 2.4% in nominal terms (or roughly equivalent to the rate of inflation), whereas both BIS and DCLG will see a reduction in funding[8]. Of the three departments, however, DfT sees the largest percentage reduction in resource spending. But because resource spending is a relatively small proportion of the DfT's overall budget the net result is positive.

However, if we take the 2013 March budget figures as the baseline, the DfT actually sees the greatest % reduction in its overall budget due to a £0.9bn fall in its 2014-15 resource budget between the March Budget and the June Spending Round. This change isn't explained in the Spending Round report and isn't consistent with the funding envelope in the 2010 CSR.

Our view is that this change could have been a result of the proliferation of small scale and short term competitive grants at the DfT, as well as one-off increases in existing grants (eg pinch point fund, cycle challenge fund, additional maintenance funding, increase in Integrated Transport Block and LSTF funding, Better Bus Areas, Green Bus Fund). Because these grants can be designed as a short term spending boost and easily discontinued between one year and the next, they may have been excluded from the Spending Round 2014-15 baseline, which does not take into account one-off and time-limited expenditure[9]. This explanation is consistent with the suspected underspend by DfT in previous years, as this could have been converted into new competitive grants subsequently.

Table two. Departmental budgets 2014-15 and 2015-16

		Budget Baseline	*SR Baseline*	*SR*	*Budget Baseline*	*SR Baseline*
		2014-15 (Budget)	2014-15 (SR)	2015-16 (SR)	% change (nominal)	% change (nominal)
Resource DEL	Transport	*4.4*	3.5	3.2	-8.6%	
	BIS	*13.8*	13.6	13.0	-4.4%	
	DCLG	*23.0*	26.8	24.6	-8.2%	
	(Local government spending)[10]		*54.8*	*54.5*	*-0.5%*	
Capital DEL	Transport	*8.9*	8.9	9.5	+6.7%	
	BIS	*2.1*	2.1	2.5	+19.0%	
	DCLG	*4.8*	4.8	3.1	-35.4%	
Capital+Resource	Transport	*13.3*	12.4	12.7	+2.4%	-4.5%

[8] DCLG's figures may be slightly misleading as the result of significant changes to the local government funding settlement. The Spending Round document therefore provides an estimate of local government spending (including changes in revenue from council tax and business rates), which gives a much lower reduction than for DCLG's DEL. Nonetheless, the fact remains that DCLG's budget is likely to fall in nominal terms.

[9] Footnote 2 in table 1 of Spending Round 2013 document.

[10] Includes Revenue Support Grant and forecasts of council tax revenues and the local share of business rates.

DEL						
	BIS	*15.9*	15.7	15.5	-1.3%	-2.5%
	DCLG	*27.8*	31.6	27.7	-12.3%	-0.4%

Another possible factor is to do with the new policy measures which were announced in 2011 and 2012. For example, the decision to scrap vehicle excise duty and defer RPI+1 increases in regulated rail and TfL fares will have put a significant dent in the DfT's revenue streams. With less money available, the DfT will have had to cut its resource budget.

Either way, this analysis questions whether, in practice, there will actually be an year-on-year increase in DfT's budget in 2015-16.

Transport Funding

Investing in Britain's future provides some detail on specific programmes which the government intends to fund from 2015 onwards. One area highlighted in the report is transport capital spending where, unusually, the Treasury has set out its long term spending plans to 2020-21. Table three presents these figures against the DfT's known budgetary plans for 2014-15 (from ***pteg***'s February 2013 Number Crunch).

Below is a summary of the key outcomes:

- The political allure of big road schemes remains strong - Highways Agency capital spending will ramp up from 2016-17 onwards; by 2020-21 it will be more than double its current level.
- HS2 spending will ramp up from 2015-16; by 2020-21, it will total around £4.5bn per year, which will significantly exceed the level of investment on the conventional rail network.
- Investment in the conventional rail network will be in line with the latest HLOS minus the efficiency savings imposed by the Office of Rail Regulation in its recent Draft Determination.
- TfL's capital grant will increase broadly in line with inflation, following a small cut in 2015-16. However, TfL will continue to have the ability to raise capital funding from other sources (including from government-guaranteed borrowing up to £600-700m per year, retained business rates and an additional grant of £800m in 2015-16 for the completion of Crossrail). Information published since the SR[11] suggests a substantial cut in TfL's resource grant (from an estimated £1.5bn in 2014-15 to £0.6bn in 2015-16).
- The allocation for local authority major schemes will jump up by 65% in 2015-16 and then remain constant in nominal terms. This will represent more than double the equivalent funding allocation during either the current or the previous Parliaments. Critically, however, the entire grant will be subsumed into the Single Local Growth Fund, which will be allocated to LEPs via a mix of formula (proportionally to population) and competitive 'growth deals'[12].
- The highways maintenance grant will increase by 25% in 2015-16 and then fall in real terms. The Integrated Transport Block will remain broadly at the same level

[11] Letter from SoS to the Mayor, dated 18th July
[12] Some of the money will also be ring-fenced to fund schemes which have already been approved by the DfT.

(in money terms) as in 2014-15. However, it will still be far below the £600m p.a. which was budgeted for in the last year of the previous government (2010-11). However, 44% of the ITB allocation will also be pooled into the SLGF, which means only £258m will be allocated on a formula basis.

- There will be an increase in the LSTF capital allocation in 2015-16, although this will be entirely subsumed into the SLGF. However, the DfT will retain control of a £78m resource grant (compared to £130m in 2014-15), which it is likely to use to leverage SLGF capital funding from LEPs to promote sustainable travel schemes.

From a local transport perspective, this analysis confirms that there will be a boost to available capital funding in 2015-16, both in relation to the last year of the current government (+28% in real terms) and the last year of the previous government (+16% in real terms relative to original 2010/11 budget)[13]. However, it's difficult to anticipate at this point what proportion of this money will end up in PTE areas and what proportion will fund transport schemes.

Table three. DfT capital budget (£million), 2014-15 to 2020-21

	2014-15	**2015-16**	**2016-17**	**2017-18**	***2018-19****	***2019-20****	***2020-21****
HS2	-	832	1,729	1,693	*3,300*	*4,000*	*4,498*
Highways Agency	*1,652*[i]	1,497	1,907	2,316	*2,614*	*3,047*	*3,764*
Net Rail	*4,157*	3,548	3,681	3,770	*3,789*	*3,824*	*3,859*
TfL capital grant	*928*[iii]	925	941	957	*973*	*990*	*1,007*
LA majors	*497*	819	819	819	*819*	*819*	*819*
LA maintenance	*779*	976	976	976	*976*	*976*	*976*
ITB	*450*	458	458	458	*458*	*458*	*458*
LSTF	*80*	100	*?*	*?*	*?*	*?*	*?*
Pinchpoint fund	*80*	*?*	*?*	*?*	*?*	*?*	*?*
RGF	*175*	*?*	*?*	*?*	*?*	*?*	*?*
Other (e.g.: cycle ambition, green bus)	*?*	*?*	*?*	*?*	*?*	*?*	*?*
	8,900	*>9,500*	*?*	*?*	*?*	*?*	*?*

***Notes**: (i) HA = 947 (CSR capital DEL) + 705 (2011 AS) ; 2012 AS assumed all resource*
(ii) Year ended 31 March 2013 from Annual Corporate Accounts
(iii) under resource spend in DfT's 2010 CSR press release, presumably in error.
(*) Beyond the usual timeframe of a Spending Review

On the other hand, the Treasury and the DfT have said nothing about what is likely to become of smaller competitive grants, such as the Pinchpoint Fund, the Green Bus Fund, the Cycle Ambition Grant or the DfT's contribution to the Regional Growth Fund. One likely possibility is that the Treasury has already lumped most of these

[13] The % change figures are calculated for ITB, major schemes and highways maintenance grants only.

smaller grants into the major schemes, ITB and highways maintenance figures . Although this would make the increase in local transport funding less impressive, our analysis suggests that it would still represent an increase on the 2014-15 budget (though not necessarily in relation to the previous government).

On the revenue side, the picture is not entirely clear. The main bit of good news is that the current rate of BSOG has been protected until 2015-16. We now also know that the DfT will manage a considerable LSTF resource grant in 2015-16. However, our earlier analysis shows that the DfT's overall revenue budget will suffer a significant cut between 2014/15 and 2015/16 (£1.2bn relative to the 2013 Budget). Although a large proportion of this will come from a reduction in TfL's resource grant (~£0.9bn), and another chunk from the LSTF resource budget, £250m are still unaccounted for. Given the structure of DfT's resource budget, however, it seems relatively unlikely that this will come out of local transport spend.

Conclusion

Although some of the Spending Round announcements arguably exaggerated the scale of the planned increase in transport spending, local transport outside London does seem to be popular with the Treasury at the moment.

On the other hand, the unexpected pooling of DfT funding into the SLGF makes it difficult to predict how much of the money available will eventually find its way into transport schemes in the metropolitan areas.

Some might argue that this is an opportunity for PTEs to capitalise on their strengths (evidence base, established prioritisation processes, competitive advantages over less specialised LTAs). However, there is also a risk that some LEPs may favour regeneration, housing or industrial policy schemes which can produce more tangible short term results. It's also unclear what weight DfT will have, relative to other government departments, in assessing SLGF bids.

Pedro Abrantes, PTEG, 11 September 2013