Growing for gold?

Analysing the tax and spend package of the 2024 Labour Manifesto

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In launching its manifesto, the Labour Party put the emphasis on efforts to boost growth. But more eye-catching were promises of some of the biggest changes to the labour market in a generation, with the aim of improving the quality of work. Proposals here included new employment rights, tougher labour-market enforcement, and an innovative approach to setting sector-wide standards in social care. This boldness was in contrast to politically-cautious approach to the public finances. Labour's plans for modest additional tax rises – £8.6 billion a year by the end of the next parliament – come on top of £23.5 billion post-election tax rises announced during the most recent parliament; together, these would take the UK's tax take to its highest level on record. The associated extra spending is concentrated in health and education, implying that a Labour government would need to deliver around £18 billion of cuts to unprotected departments such as Transport and Justice to meet its commitment to have debt falling by the end of Parliament.

Elsewhere, Labour's commitment to a child poverty strategy is welcome, and comes with a pledge to increase childcare places. But a striking absence was any comment on the two-child limit on welfare support, a policy that is set to push the majority of large families below the poverty line by the end of the decade. On growth itself, the manifesto pledges a significant ramping up of public investment – of almost £5 billion a year by 2028-29. The focus on growth is welcome but it is unclear that the scale of the pledges will be sufficient to shift the dial significantly.

Labour has chosen to take a politically cautious approach to tax and spend

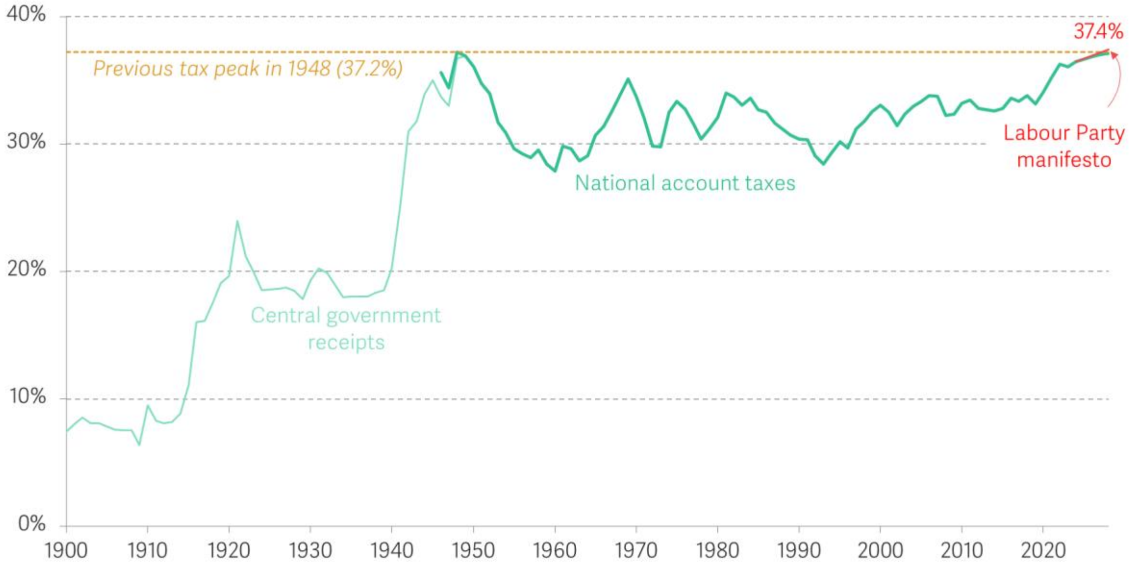
The Labour Party's manifesto suggested modest new tax rises over the next parliament. Consistent with its commitment to not raise the three largest taxes (Income Tax, National Insurance, or NI, and VAT), increases in tax are coming from closing 'non-dom' tax loopholes, reducing tax avoidance and applying VAT and business rates to private schools. In total, this would mean taxes rising by an additional £8.6 billion a year by the end of the next parliament. Coupled with £23.5 billion tax rises announced by Jeremy Hunt in the last parliament but not yet implemented, this would leave the UK's tax-to-GDP ratio rising from 36.5 per cent in

2024-25 to 37.4 per cent to 2028-29 – equivalent to £1,100 a year more in tax per household (in 2028-29 prices) – with the UK's tax take reaching its highest on record (Figure 1).

Workers might welcome the promise not to raise the three main taxes, but Labour's implicit acceptance of the future freezes in the Income Tax personal allowance mean that the personal tax bills of a typical employee earning £30,000 will rise by £180 a year by 2027-28.

Figure 1 **The tax take is set to rise to its highest on record**

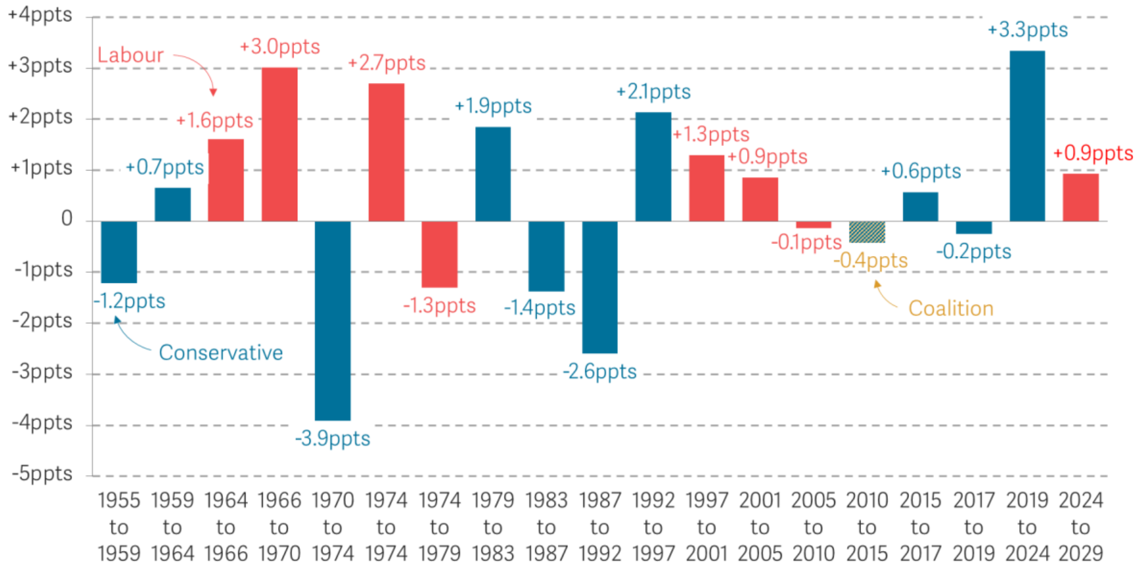
Taxes as a proportion of GDP: UK



Notes: Includes OBR projections. Final data point is 2028-29.
Source: OBR, Economic and Fiscal Outlook, March 2024; OBR, Historical public finances database, The Labour Party, Manifesto 2024.

But, as shown in Figure 2, the scale of this rising tax take in the next parliament is modest compared to the last parliament (which rose by 3.3 percentage points) and comparable in scale to the 2001-05 parliament (when it also rose by 0.9 percentage points).

Figure 2 **The scale of tax rises announced are relatively modest**
Percentage point change in tax to GDP ratio by parliament: UK



Notes: Includes OBR projections. Dates are financial years e.g. final data point is 2028-29.
Source: OBR, Economic and Fiscal Outlook, March 2024; OBR, Historical public finances database, The Labour Party, Manifesto 2024.

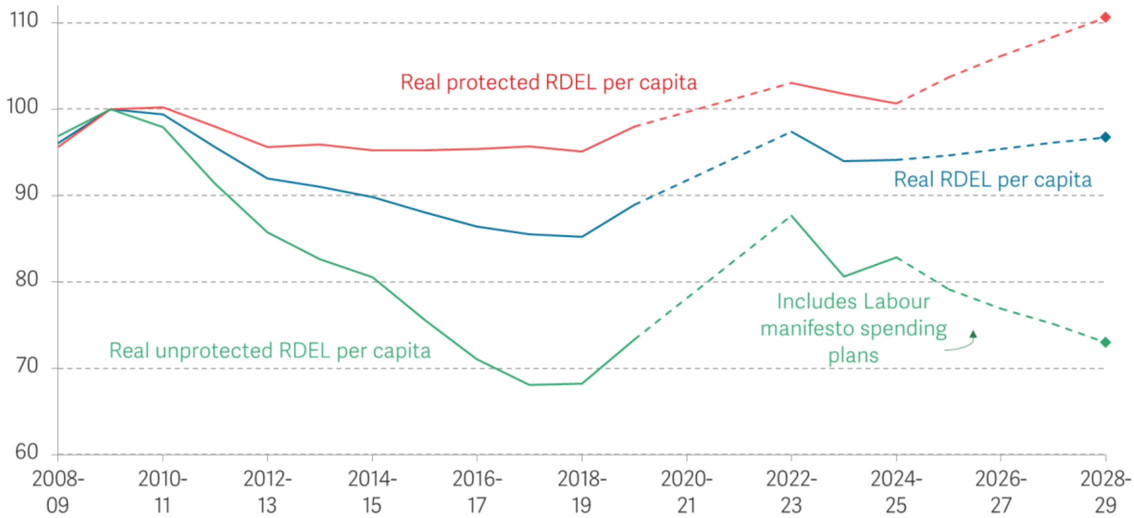
Restraint on spending suggests that a future Labour government would have to make cuts to some government departments

Labour has committed to the current Government's fiscal rule of getting debt falling by the fifth year of the forecast. But the tax and spending plans set out in the manifesto leave just £8 billion of fiscal headroom, the second smallest since the inception of the OBR in 2010. Given significant uncertainty surrounding the fiscal outlook, it would only take a relatively small change for debt to move onto an upward path, requiring Labour to look again at how it would balance the public finances within the current fiscal rules.

The majority of Labour's (modest) manifesto pledges to increase spending largely lie in departments that are already protected, such as education and Health and Social Care (Figure 3). This fact, plus the constraints of meeting its fiscal rules and the limited scale of new tax rises, mean that an incoming Labour government would likely need to deliver around £18 billion of cuts to unprotected departments, such as Transport, Justice and the Home Office. This could prove very challenging to deliver given the current state of these departments.

Figure 3 **Pledges to increase spending largely lie in protected departments**

Indices of real (GDP deflator adjusted) per-person resource departmental expenditure limits (2009-10=100), all departments, 'unprotected' and 'protected' departments



Notes: Deflated using the OBR forecast for the GDP deflator to 2024-25 cash terms. Protected budgets include NHS England, education, defence and foreign, commonwealth and development office. Figures include the impact of the Barnett formula.
Source: RF analysis of OBR, Economic and Fiscal Outlook, various; HM Treasury, Budget and Spending Review documents, various; The Labour Party, Manifesto 2024.

The manifesto pledges a significant ramping up of public investment – of almost £5 billion a year by 2028-29 – largely through its Green Prosperity Plan. This welcome extra investment should contribute to decarbonising our economy in a growth-friendly way. But it is only enough to undo a fifth of the already-announced investment cuts due to take place over the next parliament (Figure 4), and so it will do little to close the investment gap between the UK and OECD advanced economies, who spend on average nearly 50 per cent more on public sector investment than in the UK. A significant mismatch remains between Labour's plans and the scale of the task facing the next government of investing more in Britain's future.

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Figure 4 **Public investment is up, but not enough to compensate for cuts already announced**

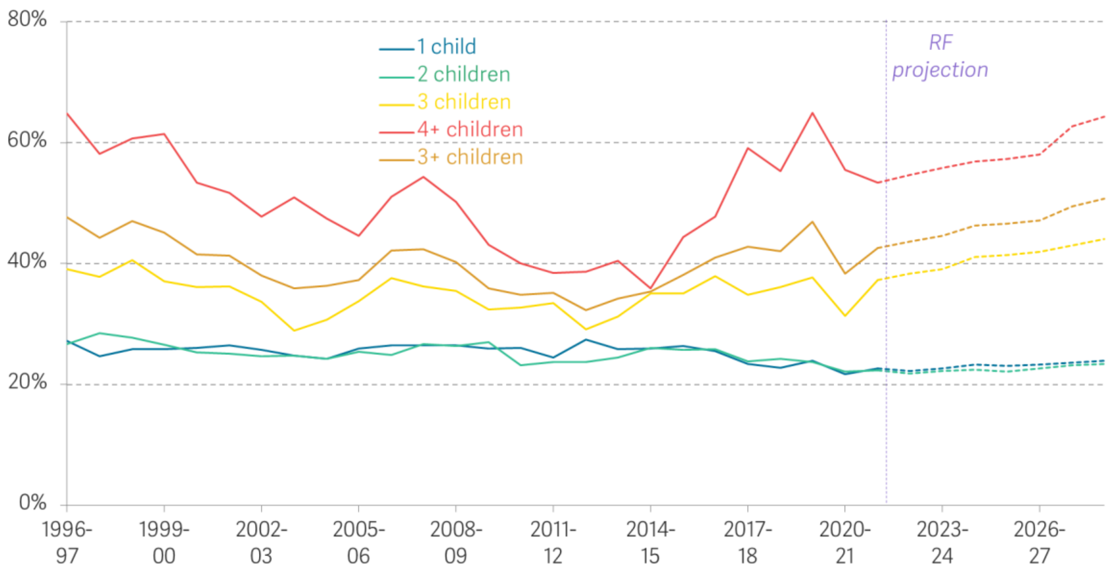
Public sector net investment (PSNI) as a proportion of GDP: UK

Source: RF analysis of OBR, Economic & Fiscal Outlook, various, Public Sector Finances Databank; Labour, Labour Party Manifesto 2024.

On benefits, the manifesto includes a welcome commitment to a child-poverty strategy, alongside increasing childcare places. But noticeable by its absence is any comment on abolishing the two-child limit on welfare support – a policy that, as shown in Figure 5, is set to push the majority of large families below the poverty line by the end of the decade.

Figure 5 **Current plans lead to rising child poverty among larger families**

Proportion of children living in relative poverty, after housing costs, by number of children in the household: UK



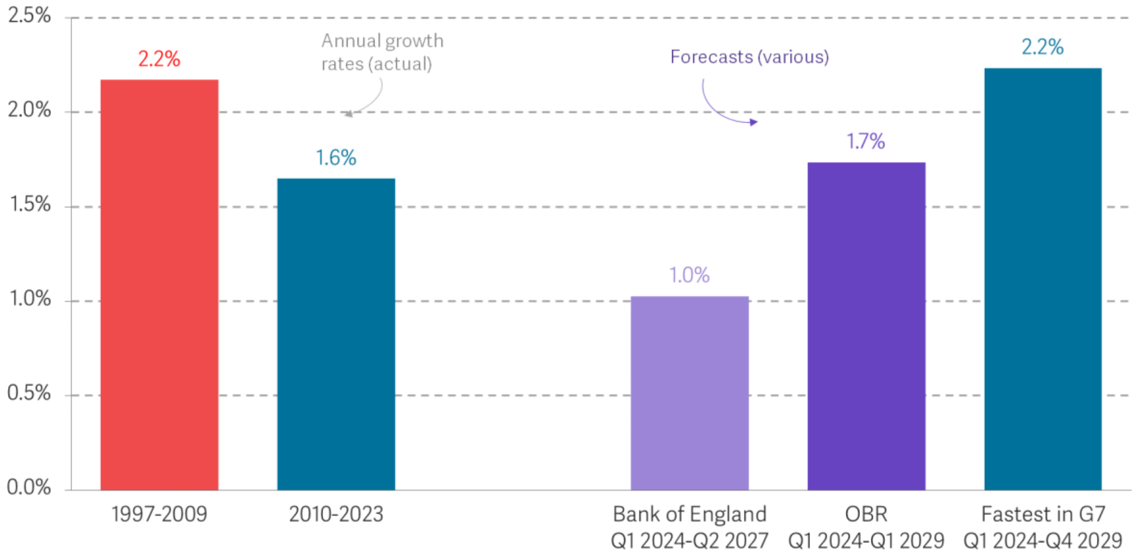
Notes: GB before 2002-03.
Source: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

Economic growth is a key goal – but it's unclear whether the measures set out will be enough to shift the dial significantly

The manifesto reiterates Labour's ambition of achieving the fastest growth in the G7. Given the UK's recent history, and how low UK growth is forecast to be compared to the rest of the G7, then it's clear that this is an ambitious target. Delivering on this would require achieving growth rates of 2.2 per cent, a level which the UK has not sustained since before the financial crisis (Figure 6).

Figure 6 **Labour's aims for economic growth are ambitious**

Annual real GDP growth rate, outturn and forecasts: UK



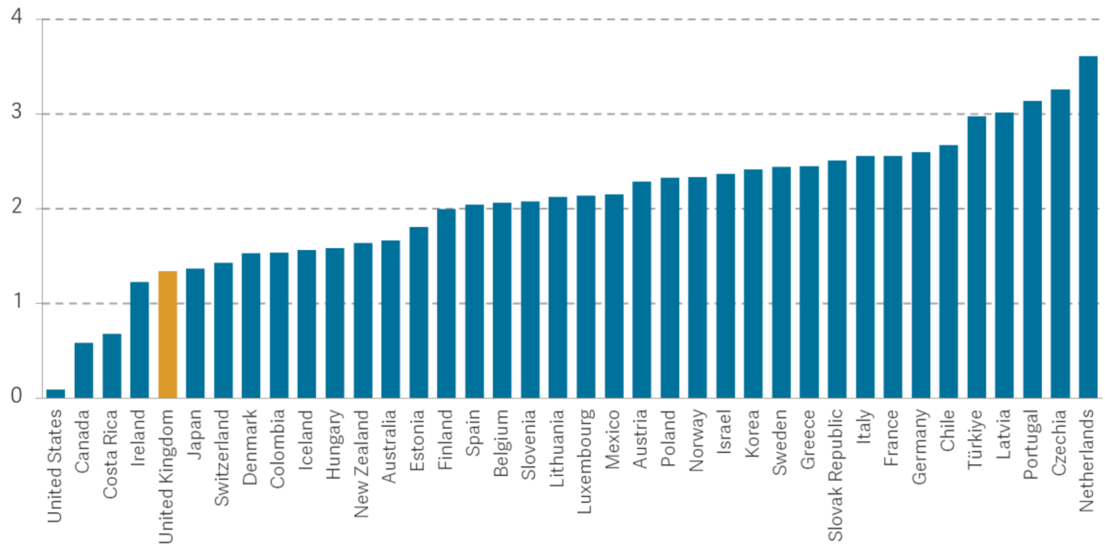
Notes: Fastest in the G7 uses the IMF WEO US growth rate over the 2024-29 period. Where Q1 is used, this represents the full year to Q1.
Source: RF analysis of ONS; Bank of England; OBR Economic and Fiscal Outlook March 2023; IMF WEO.

Alongside the higher public investment already discussed, the manifesto puts a lot of weight on stability driving faster growth. This is probably not surprising given that, since 2010, we've had Brexit, nine business secretaries, seven sets of fiscal rules, and almost annual changes to corporation tax. But the manifesto also includes a suite of growth-friendly policies, including on planning reforms, pensions investment, longer-term budgets for public R&D, and a new statutory requirement for Local Growth Plans that cover towns and cities across the country. Given the scale of the challenge, however, it's unclear that these policies are sufficiently radical to return the UK to a period of high growth.

Bold plans on the labour market are the biggest shake-up of the workplace in a generation

But despite restraint in other areas, the Labour manifesto proposes radical reforms on the labour market, including new employment rights, tougher labour-market enforcement, and plans for an innovative approach to setting sector-wide standards in social care. This focus on improving the quality of work in the UK is needed [with evidence of a deterioration in the labour-market conditions facing many workers](), particularly those on lower pay. Moreover, the UK is currently one of the least regulated among OECD countries on workers' rights, ranking 5th out of 38 countries for the ease with which employers can dismiss individual workers (Figure 7).

Figure 7 **There is plenty of scope to tighten regulation on workers' rights**
OECD index of strictness of regulation relating to dismissing individual workers (higher number = stricter regulation): OECD countries, 2019

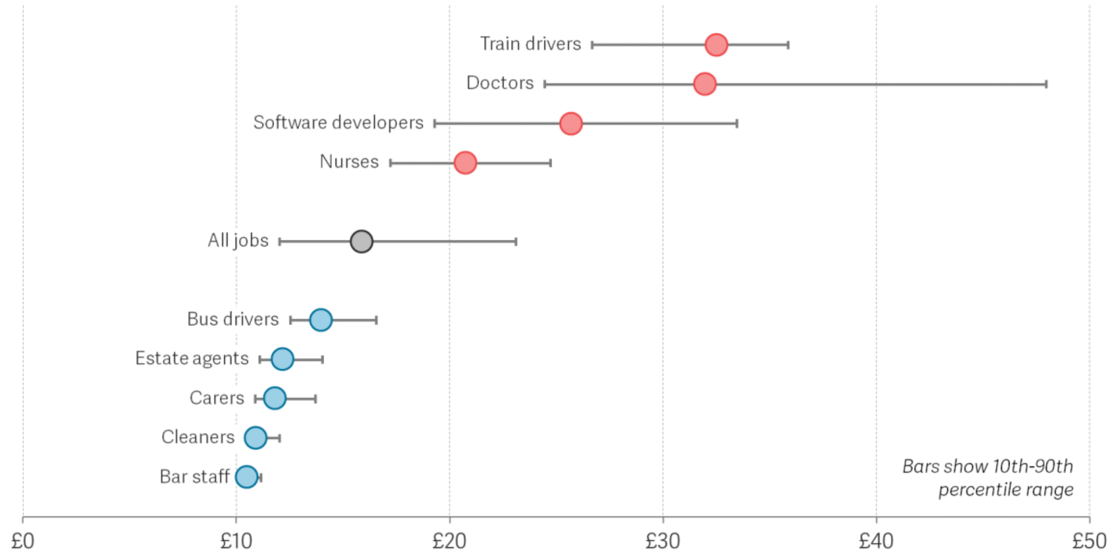


Notes: Index is a composite measure, includes qualifying periods for protection from unfair dismissal, and minimum redundancy notice periods and payments.
Source: OECD Employment Protection Index.

Improving workers' rights will need to be carefully navigated to cater to the needs of workers and employers. For example, the right to a contract reflecting regular hours worked will need to strike a balance between tackling the inappropriate use of zero-hours contracts (which at over one million are close to a record high level, despite a tight labour market) while maintaining the flexibility needed in sectors like hospitality. Similarly, 'day one' rights to improve job security should include a probationary period to avoid the risk of deterring firms from recruiting.

The proposed introduction of a new Fair Pay Agreement in social care is a welcome announcement, as care staff are among the lowest-paid workers in Britain and are often at risk of being paid less than the legal minimum wage when travel time is included. As shown in Figure 8, two-in-five care workers are currently paid less than the real Living Wage (currently £12 an hour, and £13.15 in London, compared to the National Living Wage of £11.44) – a substantial number of workers who would be set to benefit if the agreement sought to raise their pay to match the real Living Wage. This approach should also help to address the sector's chronic staff shortages, especially as demands on social care are set to increase. However, creating new labour market institutions is not straightforward, and will need to be implemented carefully, just as the Low Pay Commission was 25 years ago.

Figure 8 **Two-in-five care workers earn less than the Real Living Wage**
Gross hourly pay, by occupation (median, and 10th-90th percentile range): UK, 2023



Source: ONS, Annual Survey of Hours and Earnings.

Overall then, the Labour manifesto was bold in its approach to the labour market and improving the quality of work, but this boldness does not extend to the public finances, where Labour have taken a politically-cautious approach to tax and spend, implying slightly larger tax rises than set out by the Government last March, and a spending total that does not allow them to avoid spending cuts for unprotected departments. The manifesto also includes welcome ambition on growth. But with much of Labour's economic strategy resting on changes in the margins, rather than a step-change in investment, it's unclear whether the measures set out will be enough to end stagnation, let alone secure the strongest growth in the G7.