

Outlook and appraisal

Overview

In this special issue of the Quarterly Economic Commentary, we bring together three commissioned articles on aspects of public sector performance in Scotland. The Scottish public sector provides around a quarter (23%) of the jobs and its spending amounts to £41 billion, or just under half (48%) of Scottish GDP. The comparable UK figures are 19% and 40% respectively.¹ The public sector is therefore clearly important to the Scottish economy both absolutely and relatively. And with the Parliament responsible for more than half (55%)² of public expenditure in Scotland there is legitimate concern over the efficiency and effectiveness of spending by the Scottish Executive.

The three papers deal with different aspects of the efficiency and effectiveness debate. In the first paper Jo Armstrong considers financial management in the Scottish Executive and makes proposals for improvement. Arthur Midwinter, in the second paper, focuses on output measurement in the Scottish budget and the new efficiency targets, while Peter Wood examines whether the Executive's spending decisions match the stated priority given to growth.

Armstrong notes that in the past the Executive has been able to meet funding shortfalls in specific budget areas by making use of the end year flexibility mechanism (EYF). EYF allows for unspent funds to be reallocated at the close of each financial year and spent in other budget areas that have a high priority. However, she offers several plausible reasons why the budgetary flexibility given to the Executive through the EYF mechanism is likely to diminish in the future. A slowdown in the growth of public expenditure plus planned changes in the way budgets are managed are likely to reduce the ability to make contingency provisions for future spend within existing programmes and limit the slippage in committed capital projects.

Against that background, Armstrong suggests several options for change in budgetary and financial practices that should serve to complement developments already underway, offering the Executive more financial flexibility and increasing transparency. But such changes, along with improvements in information gathering and the development of a long-term forecasting capacity constitute, are only a necessary condition for improved financial management. What the Executive must further ensure, she argues, is a central finance function that has the people in place with the requisite skills and authority to perform the critical scrutiny and co-ordination function. A function that is essential to the efficient and effective management of the public finances in Scotland.

For Midwinter, the dropping of 138 targets in the 2004 Executive Spending Review reflects progress in the development of performance reporting. It reflects progress because now there is a greater focus in the targets on outputs and some outcomes, with much less emphasis on the traditional input and process measures. However, while commending the Executive for moving in the desired direction, Midwinter argues that substantial problems of linking budgets to results remain.

One area in which the specification of Executive targets is critical is in the increasing momentum to improve public sector efficiency. As Midwinter makes clear, the refreshed *Framework for Economic Development*, which sketches the guidelines for the Executive's priority of raising the growth of the Scottish economy, views the raising of public sector productivity as a key route to this goal, and the Executive's efficiency drive as central to that end. But he notes that the Executive sought to exaggerate the efficiency targets and claim inaccurately that the targets went further than those being pursued by the UK government. This is disappointing, because in provoking the scepticism of the press the growing trend of greater transparency in government spending may have been set back. But more crucially, the seriousness with which the Executive is pursuing public sector efficiency improvements is called into question.

The issue of transparency and the seriousness with which the Executive is pursuing a growth agenda might also be called

into question as a result of the findings of Peter Wood's paper, the final article in this special issue. A close analysis of Executive spending decisions indicates that objectives other than economic development have had first call on public spending. Wood analyses trends in the Scottish Budget since the creation of the Scottish Parliament, focusing particularly on the split between spending on activities that foster economic growth and other spending. He finds that direct or primary support to economic activity has hardly grown at all, while total spending by the Executive grew by 33%.

Moreover, within the direct support category, spending on rural economic development grew strongly, rising by 88% in real terms. Wood contends that the rural areas of Scotland continued to gain a share of economic development spending that far outweighs their population and which is not transparently related to relative 'need'. When Wood examines categories of spending that are generally regarded as important to the economy – support spending – he finds that growth is again less than total spending if the less economically significant outlays on public transport, young people's service and specific grants are excluded. Wood concludes that whether the pattern of spending growth is in line with public preferences is a matter of conjecture, but such a pattern does not fit well with the idea that economic growth comes first.

What emerges from these papers is that while progress has been made under devolution in improving the scrutiny and management of public spending in Scotland there is still much to be done to improve its efficiency and effectiveness. The Executive has, through the use of EYF to meet contingencies, effectively relied on one set of financial errors to address another, hardly the stuff of rational financial management. In seeking to exaggerate its efficiency targets it has called into question its commitment to improving public sector productivity, while the analysis of spending patterns raise further doubts about the priority it is actually giving to growth. Only greater financial transparency and the development of a stronger central Treasury function within the Executive might begin to dispel such doubts.

Endnotes

1. J. Dewar (2005) *The Size of the Public Sector*, Scottish Parliament Information Centre Briefing 05/19, 31 March.
2. Scottish Executive (2004) *Government Expenditure and Revenue in Scotland 2002-2003*.