Home Office

HOME OFFICE EVIDENCE TO THE SENIOR SALARIES REVIEW BODY

2016-17 PAY ROUND

Contents

I. Executive Summary

1. Police workforce reforms implemented by this government have focussed on ensuring that officer pay reflects the competence, skills and professional development of officers in a way that is fair and sustainable, while giving chief constables and Police and Crime Commissioners (PCCs) the flexibility they need to lead their forces and manage their resources more efficiently. Around 80% of police expenditure is on workforce costs. Therefore, reforming the way that officers and staff are remunerated remains key to delivering transformational change and value for money.

2. In the recent Spending Review and Autumn Statement, the Chancellor confirmed that overall police spending will be protected in real terms[1] over the Spending Review (SR) period to enable the police to continue to adapt to emerging crime threats, and to train more firearms officers, while taking further steps to improve efficiency. This will include a renewed focus on workforce reform.

3. Ministers remain committed to the Winsor Review's principles and objectives, in particular linking pay to skills and contribution (reflecting wider government policy), and modernising management practices. We are now looking at what scope there is for making further improvements over the next few years through changes to pay and conditions; in particular, where they could provide further incentives and levers for improving leadership and professionalism and opening up police career pathways.

4. Overall, the state of the police workforce remains healthy. The proportion of frontline officers has risen, workforce diversity continues to increase and there are no emerging concerns around recruitment or retention.

5. There is a continued need for wider public sector pay restraint, as set out in the Chief Secretary to the Treasury's letter to all pay review body chairs and in the economic evidence submitted by HM Treasury, which is attached at Annex A.

6. As set out in the Home Secretary's remit letter, you have been asked to consider the following for the 2016-17 pay round:
   - How to apply the pay award for 2016-17 within the limits of public sector pay restraint, in accordance with the Chief Secretary to the Treasury's letter to pay review body chairs. This includes consideration of evidence on the targeting of particular groups;
   - Whether any adjustments should be made to London and South East allowances in light of further evidence put forward by employers.

7. Finally, the remit letter asked that these matters for recommendation should be considered in the broader context of the work currently being undertaken by the College of Policing, with policing partners, to take forward the recommendations of the leadership review. This includes a review of rank structures and will look at the way in which skills are rewarded. This work will inform the development of longer-term pay strategy.

[1] An increase of £900 million cash by 2019-20

Summary pay proposals

8. In this context, and taking into account the evidence presented in this document, the Senior Salaries Review Body (SSRB) are asked to consider the following proposals for 2016/17:

    - a 1% consolidated increase in basic pay at all pay points and for all chief officer ranks;
    - pending the police led review of London and South East pay, to consider whether there is any compelling evidence for interim measures at local level and make recommendations accordingly, according to the conditions set out at paragraph 57;

9. This is consistent with proposals included in evidence to the Police Remuneration Review Body (PRRB). The full context and rationale for these proposals is set out below.

II. Police pay context

Police pay bill and funding

10. Following the June 2010 Budget, the Spending Review (SR) published in October 2010 set out the spending reductions required to deliver the government's consolidation plans through to 2014 to 2015. The Spending Round 2013 set out the further consolidation plans for 2015 to 2016. Managing public sector pay continues to be central to the government's plans for fiscal consolidation. The Autumn Statement 2014 confirmed the government would need to continue to reform, and take tough decisions on public sector pay, while it continues to reduce the current budget deficit.

11. The police officer pay bill for the financial year 2015/16 is around £6.6 billion. The chief officer pay bill is around £0.03bn. This includes employer pension contributions which represent 21.3% of salary costs and National Insurance contributions[2]. The effect of National Insurance (NI) contributions on salary costs will change following the end of contracting out. We are still appraising the effect that these changes will have on the police pay bill. At present, NI costs represent 8% of the total pay bill.

12. The pay bill constitutes a non-ring fenced proportion of the overall police grant to each force. This means that forces already have more freedom than other sectors about how they spend it because PCCs are not under direct ministerial control. Therefore, the affordability of the pay bill will vary by force and over time, depending on other factors and spending decisions. Any saving from the pay bill over the SR period would be retained and reinvested by forces.

13. In the Spending Review and Autumn Statement 2015, the Government announced that it will protect overall police spending in real terms over the SR period, an increase of £900 million cash by 2019-20. This provides funding to maintain overall police force budgets at current cash levels. The government will allocate additional transformation funding to those forces which have strong proposals to support efficiency and reform and to help transition to new funding arrangements in future. This funding will also allow forces to train more firearms officers to ensure the country extends its capability to protect its citizens from terrorist threats.

14. The Home Office proposals outlined in this document comply with the wider conditions on public sector pay and, if implemented, will be affordable for Government and for police forces within wider public sector pay policy.

Police workforce reform

15. Further, deeper reform is necessary to create a more flexible, skilled and increasingly professional workforce to deal with changing crime demands. The recent SR settlement has ensured that the police have the resources they need to drive this forward with renewed energy over the next few years. The Government wants to see police ranks opened up with flexible entry and exit paths, diversity of experience and backgrounds amongst police leaders encouraged, and a culture of challenge, particularly in the senior ranks, developed. The Home Office is providing a suite of tools for the police to transform and create a more flexible workforce, but how they are used is a matter for chief officers in collaboration with their PCCs.

[2] without pensions and NI contributions, the chief officer pay bill is around £0.02bn

16. The future of modern policing will require new types of leaders. That means much more movement both in and out of policing, at every level, to develop and demonstrate diverse leadership skills. There are undoubtedly very talented and capable police leaders in forces. But a diversity of experience at the top of the police will strengthen the leadership and foster police forces that are more connected to the communities they serve.

17. The Leadership Review, published by the College of Policing in July has ten recommendations to open up police leadership. These include implementing a culture of challenge at the top of forces, introducing career flexibility, embedding the Code of Ethics in selection processes and reviewing police powers in some roles so they do not block police staff appointments. The review will ensure that serving officers will have access to opportunities that will give them a broader perspective so that they can further develop and will ensure that we have the chief officers we need in the future, with the skills and experience necessary to succeed. This will be achieved by looking at not only developing the talent within the police, identifying good officers earlier and providing them with the opportunities to develop their skills, but also looking at the way in which people enter the police to attract a diverse a range of people and talents as possible.

18. The future success of the police is dependent on attracting the best and brightest to careers in the force. The three direct entry schemes offer the opportunity to widen the talent pool from which we attract our police officers and will bring in people from a diverse range of backgrounds. The fast track to inspector and superintendent scheme is aimed at those who have the potential to reach the highest ranks in the police. Forces have been working with the College of Policing to put in place a robust selection process to ensure that only those who can meet the high standards required are successful, particularly at superintendent level. It is right that forces only consider those who they are confident can complete the demanding training programme and go on to be excellent police leaders, bringing a fresh perspective and benefitting their colleagues and the public.

19. Other aspects of reform which will have an impact on all ranks are as follows:

- The Government believes that volunteers should play a greater role in the future, which is why on 9 September a consultation was launched to extend the powers of both staff and volunteers, to enable them to support officers more effectively in keeping their communities safe.
- Police Now, a flagship Metropolitan Police scheme which is supported by Home Office funding, is increasing the number of black and minority ethnic (BME) recruits to the police, furthering the aim of building police forces which reflect the communities they serve.
- As the first professional body for all of policing in England and Wales, the College of Policing develops standards for policing based on strong evidence so that in future, police practice is always based on evidence, and not habit. The College then helps police officers and staff meet those standards throughout their careers. Publishing the first ever Code of Ethics ensures that all officers and staff have a clear code against which to measure their behaviour. The College have been working with forces to embed the Code.
- Following an end to end review of the police disciplinary process by Major-General Chip Chapman the Home Office also introduced specific changes to the police disciplinary system which included holding police misconduct hearings and appeals in public, and introducing legally-qualified persons to chair the panel in misconduct hearings.
- The current Home Office consultation on measures to bring fire and police closer together will also give PCCs and chief constables greater flexibility in meeting the demands on police forces.

Pay reform

20. The longer term aim is for a modern pay structure that is strongly aligned to roles, competence and skills by the end of the SR period instead of one rooted in time-served progression. This will build on a period of radical and wide-ranging pay and conditions reforms in the wake of the Winsor Review which began in 2012 and which have not yet reached completion.

21. The phasing out of automatic pay progression will be completed for all ranks by 1 May 2016. From that point on, progression for all officers will be entirely conditional on achieving a satisfactory annual performance appraisal. The linkage of pay progression to performance was implemented for sergeants and chief inspectors as of 1 May 2014. From 1 May 2016, progression for constables will also cease to be automatic. Incremental pay progression currently represents an annual increase in pay of between 2% and 7%, depending on rank and experience, with an associated rise in employer pension contributions and National Insurance payments.

22. Work is also being taken forward by the College of Policing to develop Threshold Assessments, including Foundation Assessments for constables at point 3 on the pay scale. This will mean that officers must pass a competence assessment, including proof of continuous professional development, in order to progress to point 4. Together with the introduction of performance assessment standards, threshold assessments will make the first strong link between pay and competence and will drive increased professionalism through the inclusion of Continuous Professional Development elements in the assessment criteria. The new Foundation Threshold Assessments are due to be implemented from September 2016.

23. Some original elements of the threshold work are likely to be overtaken by Leadership Review recommendations, in particular the concept of an 'Advanced Practitioner' status and the recommendation for a review of ranks and hierarchies which is being taken forward by chief constables and the College. This police-led reform will set out options for a flatter rank structure to empower individuals and improve communication between ranks. A rank structure based on levels of competence and skills rather than the current linear hierarchy will provide a stronger basis for objective assessment of whether someone can carry out a role at a sufficiently high level and in a way that reflects the organisation's values. It will also encourage a more open, aspiring culture and support a modern pay structure that recognises competence and skills, rather than time served. We expect to see early findings on these recommendations in January and we will then be able to determine the detail of any consequences for pay structures in future years. However, it is clear that getting existing measures right will be critical in implementing more radical changes in future and we expect a renewed drive from forces to ensure that performance links to pay and threshold testing are fully embedded and that officers at all levels are engaged with these reforms.

State of the workforce

24. There is still no evidence of any widespread recruitment or retention issues for the police, including at chief officer rank. In addition to the headline workforce information provided below and the detailed data sets provided separately to the police pay review bodies (see paragraph 46), further detailed information about applications, recruitment and promotions will be provided in evidence from police partners.

Appointments

25. Since their introduction in November 2012, PCCs have successfully appointed 32 chief constables (as at November 2015). Six women have been appointed as chief constable since November 2012 (there are currently six female chief constables in England & Wales and one temporary chief constable).

26. As part of their role in supporting PCCs and chief constables the College of Policing has developed guidance and a toolkit for making senior appointments. The College also supports PCCs by providing details of career history, skills and qualifications, in order to ensure that PCCs have as much information they need to appoint chief constables. In their Leadership Review, the College also made a recommendation to create more flexibility in police careers and we will support it in considering other options to encourage more movement at this level. The review also recommended advertising all vacancies for recruitment and promotion nationally.

Skills and capabilities

27. We continue to work with police partners, including chief constables, the College of Policing and the National Police Coordination Centre to improve national oversight of key capabilities which may require specialist skills now and in future: in particular, those needed to tackle the national threats identified in the Strategic Policing Requirement (SPR) such as terrorism, serious and organised crime, cyber, public order, and civil emergencies. The SPR Programme Board is a police led initiative chaired by Chief Constable Peter Vaughan, which provides a vehicle to hold national policing leads to account for the provisions to tackle the national threats within the SPR and ensure there are sufficient resources available. The National Police Coordination Centre are undertaking a quarterly data collection exercise which identifies the number of officers in specialist roles. This work gives policing leaders a collective understanding of the gaps in capabilities at local, regional and national levels while enabling them to make well informed decisions regarding the provision of specialist units and where gaps exist.

Diversity

28. The police have made real improvements in diversity and the latest workforce figures show that the long-term upward trend in numbers of minority ethnic and female officers is continuing. There has been an increase of 3.9% in the number of minority ethnic officers and an increase of 0.2% in the number of female officers compared with last year[3].

29. Although progress is being made in some areas, there is clearly more to do. BME officers remain under-represented at senior ranks, with 3.4% of officers at the rank of chief inspector or above at 31 March 2015 compared with 6% at constable rank. The proportion of those in senior ranks (chief inspector and above) who were women was 21.4% (up by 1.9 percentage points since March 2014), compared with 30.2% of women at constable rank (up by 0.1 percentage point since March 2014). Force returns show that there are just 3 BME officers at chief officer rank compared to 5 last year and there are still no BME officers at chief constable rank. There were 43 female chief officers (ACC, DCC and CC), representing 21.4% of total chief officers, which is an increase from 15.2% in 2010.

30. Innovative schemes such as Direct Entry, Fast Track and Police Now (see section on Police Workforce Reform) are making the police workforce more diverse than ever before; showing

[3] On 31 March 2015, there were 6,979 minority ethnic officers, representing 5.5% of all officers. There were 35,738 female officers, representing 28.2% of all officers.

that we can attract the brightest and best into policing, whilst introducing new perspectives into policing some of the country's most challenging neighbourhoods.

31. The College of Policing is taking the lead as the professional body for policing working with forces to deliver improvements. It has published advice on the bold use of positive action to increase the recruitment but also crucially the retention and progression of officers from under-represented groups. The College is also supporting all forces with diversity action plans and positive action events for the Fast Track programme.

32. The Metropolitan Police Service (MPS) has shown how creative forces can be within existing positive action provisions. With the support of the Mayor's Office for Policing and Crime it introduced a London residency criteria for new recruits which is helping the force become more representative of the communities it serves. Figures released in September showed that in the three months from June to August 26% of new MPS recruits came from a black or minority background, which is more than double the current proportion of BME officers in the MPS.

Wellbeing and sickness management

33. Chief constables, working with directly elected PCCs, are responsible for managing the police workforce effectively and ensuring the welfare of all officers and staff.

34. The proportion of officers absent on short/medium term and long term sick leave are published by Her Majesty's Inspectorate of Constabulary (HMIC) in their Value for Money profiles. This data indicates that while long-term sickness rates remained steady between March 2013 and March 2014, it increased slightly in March 2015 (up from 1.4% of all officers on long term sickness to 1.7%). From the evidence available, there are no issues emerging at chief officer level, but we expect PCCs and chief constables to continue to monitor this locally and contribute to national data where possible. We are aware that police partners have commissioned various pieces of research on wellbeing and engagement and look forward to seeing their findings.

35. The Government recognises the importance of police welfare. In October 2014, we allocated £10m to help support emergency services personnel and volunteers, focused on mental health, physical recuperation and bereavement support for those who need it. In addition, the College of Policing is supporting police forces in a range of measures to help reduce sickness and stress. The College will continue to identify issues relating to the occupational health and safety of professionals working in forces, including on high risk roles, and will work with the national policing lead for workforce development to address them.

36. In relation to Limited Duties measures implemented last year, we expect forces to continue to monitor equalities issues now that they have started to use the new definitions and procedure for the management of medical capability issues. SSRB will be kept informed of any pay-related issues that arise once these measures start to take effect. We have committed to review the Regulations on Limited Duties in September 2016 which will provide a more formal opportunity for review.

37. A Police Advisory Board (PAB) working group continues to provide advice on chief constables' proposals for the implementation of Capability Dismissal provisions.   We have committed to introduce provisions in legislation once the proposal is finalised in a form that forces can use. Like Limited Duties reforms, this will apply to chief officers as for other ranks.

Pensions

38. The framework for new police pension arrangements from 1st April 2015 was announced by the Home Secretary in September 2012. In line with wider public service pension reform, this introduced career average pension arrangements and higher employee contribution rates. Increases in employee contributions phased in between 2012 and 2014 have delivered savings of around £150m per year - a fairer balance between officers and other taxpayers.

39. The new arrangements include a normal pension age of 60. Police officers will continue to retire earlier than most public servants, who will have a normal pension age linked to state pension age. The framework also includes continued flexibility for officers to be able to retire with an immediate pension from age 55.

40. Three pension schemes currently apply to police officers:

- the Police Pension Scheme 1987 (PPS), which closed to new members on 6 April 2006;
- the New Police Pension Scheme 2006 (NPPS), which was available to all new entrants from 6 April 2006 and to any officers who chose to transfer from the PPS during a 2006 options exercise; and
- the Police Pension Scheme 2015, which has been available to members from 1 April 2015.

Protected members

41. The 1987 and 2006 schemes have closed, except for those within 10 years of retirement, who are protected. They will be entitled to remain in their current police pension scheme beyond 2015. This applies to officers who, on 1st April 2012, were within 10 years of their normal pension age (age 55) in the NPPS or within 10 years of maximum pensionable service (30 years' service) for those in the PPS. This means that almost all pensions in payment for the next 5-10 years will continue to be from the old schemes.

Other developments

Police officer overtime and payment for annual leave

42. Following the Employment Appeal Tribunal for Bear Scotland vs. Fulton, we have been working with chief constables to determine the implications for police officer pay and conditions. Any amendments are likely to require changes to legislation and the pay review bodies will be kept updated on progress.

Children & Families Act 2014

43. In line with wider labour market reforms, the government remains committed to reflecting provisions of the Children and Families Act 2014 for police officers, in particular those sections relating to arrangements for parental leave and adoption leave. Joint work is currently being taken forward by police partners to determine the operational impact and how this might best be implemented in forces. Once final proposals have been developed, we expect chief constables to recommend a way forward and if further legislative changes are required, we will consult partners on amendments to Police Regulations and determinations.

Future requirement for gender pay reporting

44. On 25 October, the Prime Minister and Women and Equalities Minister Nicky Morgan announced that the Government will extend its plans for gender pay gap reporting beyond private and voluntary sector employers to include the public sector, including the police workforce. We will provide further information to police partners and to the police pay review bodies as it becomes available.

Re-Alignment of London Weighting Payments

45. Last year, PRRB recommended the realignment of London Weighting payments, currently paid in July, with the main pay award on 1 September 2016. We intend to implement this as agreed for all ranks and will consult police partners on the way in which this should be implemented.

Data provision

46. The number of police officers at each pay point by rank, as well as the number receiving allowances and overtime have been provided to the pay review body secretariat separately through the annual Police Workforce Census. Additional tables from the Annual Data Requirement have also been provided and we have provided some headline data in this document.

47. We have worked with partners over the course of the year to achieve more clarity on roles and responsibilities around data provision and to improve current collections. Good management data is an essential tool for forces if they are to effectively monitor the productivity and efficiency of their workforce and can be useful in assessing the impact of changes. For example, we would expect forces to have good systems in place to monitor working hours, pay, overtime, sickness etc. However, we recognise that where data is not already standardised through existing collections, national collections can be more difficult, given the variety and state of interoperability of force HR systems.

48. We are working with forces through the Police Data Requirement Group (led by the Home Office and comprising policy leads, force representatives and HMIC) and as part of the pay review body process to identify how the quality of existing collections can be improved, to streamline the census process for forces and to make all partners aware of the importance of having national data on wellbeing and engagement, including exit data. In particular, it is disappointing that Northumbria, Nottinghamshire and Cumbria were unable to return any census data this year and we will work with these forces and national police leads to identify issues and resolve them where possible.

III. Pay proposals

Consideration of pay targeting

49. Recognising the strong steer in the Chief Secretary to the Treasury's letter to the pay review bodies this year, we have carefully considered all possible options for targeting pay to better reflect those whose skills are most in demand and support the delivery of public services. However, after examining all available evidence, we have concluded that a variable award would be extremely challenging to implement in 2016-17 and that targeting specific groups at this critical stage of reform could be counter-productive.

50. The potential for pay to be used to address recruitment and retention issues or skills gaps in the police is limited at this stage in the reform process. The available data shows no obvious recruitment and retention issues at present, and where we know that there have been historically low application rates for some chief officer roles in some forces, there is still no evidence that pay is the determining factor. In addition, the kind of robust frameworks, standards and management skills which would allow variation between different groups within ranks have not yet been fully developed. Systems which will help do this in future are still at an early stage of implementation.

51. Although we expect that most forces meet national performance assessment standards and should be able to withhold pay increments for poorly performing ACCs, the majority are not yet at a stage where they would be able to reward exceptional performers in a different way from good or satisfactory performers. The rollout of performance assessment standards is at a critical and early stage and will need to be more fully embedded before forces are able to do this.

52. In general, we acknowledge that any pay award in addition to performance-linked pay progression would need to apply to all officers, since there is currently little justification for withholding the award from poor performers. We accept the view expressed by the police pay review bodies last year that poor performance measures are intended as a supportive tool to help improve performance, and that denying any uplift to this group in addition to withholding pay progression may disincentivise managers from using them.

53. **Taking into account these factors and all available workforce evidence, we therefore propose a 1% consolidated increase to all ACC pay scale points and to DCC and CC spot rates for 2016-17, consistent with the recommendation to the Police Remuneration Review Body. Alongside this, we would expect a continued emphasis on driving forward radical workforce reform in forces, including ensuring that ongoing changes are fully embedded.**

54. This would represent an overall estimated increase[4] to the police pay bill of around £0.24m[5] over the 2016-17 police pay year. We believe that this is affordable for forces, given the additional investment in policing through the recent SR settlement.

London and the South East

55. In relation to London and South East Allowances, we await the results of the police led review of these elements of pay before coming to any conclusion on this matter. We continue to support the view that any future changes in regional allowances should be made

[4] Compared to a 0% award.
[5] Including employer pension contributions and National Insurance payments.

in a way that is consistent with the wider national framework and which supports the move towards strengthening the link between competence/skills and pay.

56. **We propose that London Weighting is maintained at the current level this year for all ranks since we have seen no evidence to suggest that an increase would alleviate recruitment or retention issues.**

57. **Although we are not aware of any new evidence at present, we recognise that other police partners may wish to provide more context around local issues affecting chief officer ranks and that new evidence may arise during your consideration. In the event that any new and compelling evidence is provided about local recruitment and retention issues, we ask that you carefully consider it and make recommendations if there is exceptionally strong evidence that pay would alleviate the situation. However, this will be on the condition that any such emergency measures must:**

    - **be balanced with other recommendations - the totality of recommended measures must not increase the pay bill for this remit group by more than 1% overall;**
    - **be an interim measure for a single year only, pending the police-led review of London and South East pay; and**
    - **have standard criteria and a cap on payments to keep them within affordable limits.**

Allowances

58. SSRB members should note that chief constables have indicated that they intend to put forward proposals in their evidence to PRRB to give more flexibility for forces to set motor vehicle allowance rates. We have indicated that we would support chief constables' proposals for PRRB to review and make recommendations on this, on the condition that any changes do not increase the pay bill.

Annex A – Evidence from HM Treasury

Evidence on the general economic outlook

Introduction

The UK economy grew faster in 2014 than any other major advanced economy at 2.9%, its best performance since 2005. The Spending Review and Autumn Statement set out the government's long term economic plan to fix the public finances, return the country to surplus and run a healthy economy that starts to bear down on the excessive national debt. It recognises the risks from abroad and the need to secure Britain's economic future.

Public sector pay restraint has been a key part of the fiscal consolidation so far. It helped save approximately £8bn in the last Parliament and is expected to save another £5bn in the current Parliament. At a time when further spending reductions are required to complete the repair of the public sector finances, a policy of pay restraint makes a significant contribution to protecting jobs and maintaining public services.

At Summer Budget 2015 the government announced that it would fund public sector workforces for pay awards of 1% for four years from 2016-17 onwards. The OBR estimates that this policy will protect 200,000 jobs by 2019-20. The government expects that pay awards will be applied in a targeted manner to support the delivery of public services, ensuring that flexibility exists to meet any recruitment and retention pressures.

The UK economy is fundamentally stronger than five years ago, with positive growth since the first quarter of 2013. The UK economy grew by 0.4 per cent in the third quarter of 2015 and the Office for Budget Responsibility (OBR) forecast the UK economy to grow by 2.4 per cent in 2015 overall.

Since 2010 the deficit has halved as a share of GDP and for the first time since 2001-02, the national debt is forecast to fall in 2015-16, meeting the target set out in 2010. However, risks remain to the recovery, including from slower growth in the global economy. Debt stands at its highest share of GDP since the late 1960s, and the deficit remains among the highest in advanced economies. At Spending Review and Autumn Statement, the government set out the action it would take to complete the job of repairing the public finances started in the last Parliament. The government will reduce the deficit at the same rate as in the previous Parliament (around 1.1% of GDP a year on average) to reach an overall surplus of £10.1bn in 2019-20. Running a surplus on the headline measure of borrowing is the most reliable way to bring down debt as a share of GDP in the long term.

Inflation is forecast by the Bank of England and OBR to remain low for rest of the year, before returning gradually to the 2 per cent target in the medium term. The OBR forecast inflation of 0.1 per cent in 2015 and 1.0 per cent in 2016. The Bank of England's latest inflation forecast, published in the November Inflation Report has been revised down compared to the August report. The Monetary Policy Committee (MPC) expect inflation at 0.1 per cent (down from 0.4 per cent) in the year to Q4 2015, 1.25 per cent (down from 1.6 per cent) in the year to Q4 2016, and unchanged at 2.1 per cent in the year to Q4 2017.

Headline employment and unemployment figures were strong in 2013 and 2014. This trend has continued in 2015 with employment almost continuously rising, reaching a record high in the three months to October of 31.3m, at a record rate of 73.9 per cent. The OBR expects employment to increase by 1.1 million over the forecast period, representing employment growth of 3.5 per cent. Unemployment fell by 244,000 in the year to Aug-Oct 2015 to a level of 1.71m. The unemployment rate in the three months to October 2015 stood at a 9 year low of 5.2 per cent, down from the peak of 8.5 per cent in the three months to November 2011. Real wage growth has remained at pre-recession rates. In the three months to October, total pay grew by 2.4 per cent in both nominal and real terms, compared to the same period last year. Regular wages grew by 2.0 per cent in nominal terms and 2.1 per cent in real terms. Total pay in the private sector grew by 2.7 per cent, while in the public sector (excluding financial services) it grew by 1.6 per cent. Average earnings have outstripped inflation for 13 consecutive months, the longest period of real earnings growth since before the recession, and are forecast by the OBR to continue to grow faster than inflation for the entire forecast period.

Growth

1. In 2008 the UK was hit by the most damaging financial crisis in generations. Between Q1 2008 and Q2 2009 the UK economy contracted by 6.1%, greater than the reductions in growth in the US, France, and Canada.
2. The government's long term economic plan has secured the recovery. The government's fiscal responsibility has allowed monetary activism to support demand in the economy alongside repair of the financial sector. This has been supported by supply-side reform to deliver sustainable increases in standards of living.
3. UK GDP growth has been positive since the first quarter of 2013 and GDP is now 6.1% above its pre-crisis peak. Growth in 2014 was 2.9%, above the Office for Budget Responsibility's (OBR) March forecast of 2.6%. The UK economy grew by 0.4 per cent in the third quarter of 2015, following 0.5 per cent growth in the second quarter. The recovery is broad-based with widespread growth across all major sectors since the start of 2013, and production, services and construction all growing in the third quarter on a year earlier. The OBR's forecast at Autumn Statement 2015 confirmed the UK recovery is well established with growth of 2.4% in 2015 and 2016 at 2.4%,before rising to 2.5% in 2017.
4. However, external risks remain, reinforcing the case for stability in the government's long-term economic plan. The global economic recovery remains uneven and the risks from the world economy demonstrate the need to continue to fix the economy to ensure the UK can deal with risks from abroad.
5. As a part of its economic policy, the government has announced its intention to improve the UK's productivity performance. Improving productivity is key to increasing living standards and delivering strong growth. The government has published a productivity plan ('Fixing the foundations: Creating a more prosperous nation') which tackles the UK's serious long-term challenges, with major reforms to improve the UK's infrastructure, tackle failures in the skills system, improve the planning system, encourage long-term finance for productive investment and give cities the governance and powers they need to succeed.

6. In the Autumn Statement the government announced further measures to improve productivity in the UK including protecting per pupil funding for schools, providing an additional £1.3 billion (until 2019-20) to attract new teachers into the profession, protecting today's £4.7bn science funding in real terms for the rest of the Parliament, investing up to £6.9bn in the UK's research infrastructure up to 2021; and proposing a new University focusing on Engineering, to be located in Hereford.

Figure 1: Forecasts for GDP growth 2015 to 2017

Forecasts for GDP growth (per cent)	**2015**	**2016**	**2017**
OBR (Summer Budget 2015)	2.4	2.3	2.4
IMF WEO (July 2015 update)	2.4	2.2	2.2
Avg. of independent forecasters (August 2015)	2.6	2.4	2.4

Inflation

7. November's annual CPI inflation rate was 0.1%, up from -0.1% in August. External factors, such as oil and commodity prices, continue to exert significant downward pressure on inflation. Recently low inflation is good news for working families, helping their budgets stretch further with lower food and fuel costs. In the year to November 2015, food prices fell by -2.7% and prices of motor fuels fell by -12.9%.

8. Compared to the Bank of England's August 2015 *Inflation Report*, the outlook for inflation in the August report has been revised downwards. The MPC judged that CPI inflation is likely to remain close to zero in the near term, before rising as past falls in energy prices begin to drop out of the annual comparison. The Monetary Policy Committee (MPC) expect inflation at 0.1 per cent (down from 0.4 per cent) in the year to Q4 2015, 1.25 per cent (down from 1.6 per cent) in the year to Q4 2016, and unchanged at 2.1 per cent in the year to Q4 2017.

9. Inflation is forecast by the Bank of England and OBR to remain low for rest of the year, before returning gradually to the 2 per cent target in the medium term. The OBR forecast inflation of 0.1 per cent in 2015 and 1.0 per cent in 2016.

Figure 2: Forecasts for CPI Inflation 2015 to 2017

Forecasts for CPI Inflation (per cent change on a year earlier)	**2015**	**2016**	**2017**
OBR (Autumn Statement 2015)	0.1	1.0	1.8
IMF WEO (October 2015)	0.1	1.5	2.0
Avg. of independent forecasters (December 2015)	0.1	1.3	1.9

Affordability and Fiscal Strategy

10. Since 2010 the government has taken action to cut the deficit which has more than halved as a share of GDP from its 2009-10 post-war peak. However, the job is not yet done. The deficit remains high compared to advanced economies and public sector net debt as a share of GDP has more than doubled since the pre-recession period. The government remains committed to eliminating the deficit and to getting debt as a share of GDP on a declining path across the forecast period to return the public finances to a more sustainable position.

11. At Summer Budget the government announced its intention to reduce the deficit at the same average rate as over the previous Parliament. That means reducing the deficit by around 1.1 percent a year on average over the next four years. The government is maintaining this same pace of deficit reduction and has taken the decisions necessary to finish the job of repairing the public finances. Public sector net borrowing as a share of GDP is forecast to fall year-on-year across the forecast period and the government is expected to achieve a surplus of £10.1bn in 2019-20.

12. However continued action will be required in order to bring debt down to more sustainable levels. Last year, net debt as a share of GDP reached its highest level since the late 1960s. By 2020-21, it is still forecast to be 71.3%, significantly above the pre-recession level in 2007-08. High debt increases the UK's vulnerability to future shocks. Evidence suggests that at higher debt levels, the scope for fiscal policy to stabilise the economy is reduced.

13. A strategy for debt reduction must also take into account the possibility of future economic shocks. Independent monetary policy now delivers low and stable medium-term inflation to the benefit of the whole economy. This contrasts with the experience after World War II, when very high inflation, together with artificially low interest rates, played a major role in reducing debt. The UK economy has been subject to relatively frequent shocks in the past, and though their nature and timing are unpredictable, responsible fiscal policy should allow for them. Once future economic shocks are allowed for, running a deficit to finance capital investment (balancing only the current budget) and relying on trend economic growth is insufficient to bring down debt, as set out in HM Treasury analysis at Budget 2014. In a low inflationary environment, with economic shocks, the most reliable way to bring down debt as a share of GDP is to run an overall surplus in normal times. Substantial debt reduction in future will depend on responsible management of the public finances and sustainable economic growth.

Proposed new Charter for Budget Responsibility

14. On 14 October 2015, Parliament approved the government's updated Charter for Budget Responsibility. The new fiscal rules commit the government to delivering a surplus by the end of the Parliament, and every year thereafter when the economy is in normal times, entrenching a commitment to long-term fiscal sustainability. The Charter sets out:

    - A target for a surplus on public sector net borrowing in 2019-20, and a supplementary target for public sector net debt to fall as a share of GDP in each year from 2015-16 to 2019-20.

- A target, once a surplus is achieved in 2019-20, to run a surplus each subsequent year as long as the economy remains in normal times.

15. Under the updated Charter, the surplus rule will be suspended if the economy is hit by a significant negative shock (defined as 4 quarter-on-4 quarter GDP growth below 1%). This provides flexibility to allow the automatic stabilisers to operate freely when needed. Following a shock, the government of the day will be required to set a plan to return to surplus, including appropriate fiscal targets. The framework does not prescribe what the targets should be, allowing the government of the day to respond to the circumstances. However, the targets will be voted on by the House of Commons and assessed by the OBR.

16. The end goal is to ensure that long-term debt reduction continues, leaving the country better placed to withstand future economic shocks. Returning to a surplus in normal times will provide the government of the day with the fiscal space to allow appropriate action to be taken in the face of future shocks.

Labour market

17. After strong rises in 2013 and 2014, headline labour market figures slowed in the first half of 2015. 2014 saw the employment level increasing by over 600,000, and the employment rise in the first half of 2015 was 139,000, taking the level of employment to 31.0m. Since then, employment has risen to record levels of 31.3m. In the three months to September, the employment rate rose by 1.0 percentage point on the year to 73.9%, the highest rate on record. The unemployment rate fell by 0.8 percentage points on the year, and by 3.3 percentage points since the peak of 8.5% in the 3 months to November of 2011, to a 9 year low of 5.2 per cent. The OBR forecast the rate to stabilise at 5.4% by the end of the forecast period.

18. The number of vacancies in the three months to November 2015 stood at record levels, having increased by 45,000 over the year to 747,000. The number of unemployed people per vacancy fell to 2.3 in the three months to October 2015, down from a high of 5.9 following the recession.

19. Wage growth picked up in 2015, reaching levels of up to 3.3 per cent in the three months to May. The most recent data shows more moderate total pay growth of 2.4 per cent in the three months to October, in both nominal and real terms, with real wage growth remaining at pre-recession rates.

Employment and unemployment

20. Over the year to the three months to October 2015, employment grew by 505,000. The majority of this growth was among full-time employees, whose numbers increased by 348,000 on the year. The number of people in self-employment rose slightly on the year (71,000).

21. Over the year to Aug-Oct 2015, unemployment fell by 244,000 to 1.71m, down 995,000 from the peak in the three months to November 2011.

22. Long term unemployment (unemployment of 12 months or more) stood at 509,000 in Aug-Oct 2015, down by 175,000 over the year. Over 70% of the fall in total unemployment over the year came from the decrease in long term unemployment.

23. Working age inactivity (16-64) fell slightly on the year to the three months to October 2015, with the level and rate at 8.93m and 21.9% respectively. The female inactivity rate also continued to decline, dropping 0.4 percentage points on the year.

24. Youth unemployment (16-24) fell by 129,000 over the year to Aug-Oct 2015. This was primarily amongst those not in full-time education. The youth unemployment rate stood at 13.6%, down 2.9 percentage points on the year. Excluding people in full-time education, there were 416,000 unemployed 16-24 year olds, with a corresponding unemployment rate of 12.2%.

25. The claimant count fell by 112,400 in the year to November 2015. The claimant count rate stood at 2.3%, the lowest level since February 1975. Figure 4 summarises these statistics:

Figure 4: Labour market statistics summary (Levels in 000s, rates in %)*

	2010	2011	2012	2013	2014	Aug-Oct 2015
Employment level (All aged 16 and over)	29,228	29,376	29,696	30,043	30,726	31,302
Employment rate (All aged 16-64)	70.4	70.3	71	71.5	72.9	73.9
Unemployment level (All aged 16 and over)	2,497	2,593	2,572	2,476	2,027	1,713
Unemployment rate (All aged 16 and over)	7.9	8.1	8	7.6	6.2	5.2
Youth unemployment level (All aged 16-24)	933	996	1005	969	783	625
Youth unemployment rate (All aged 16-24)	20	21.4	21.4	20.8	17	13.6
Claimant Count	1,496.4	1,534.4	1,585.6	1,421.0	1,037.6	796.2

* The latest public and private sector employment figures available are for the third quarter of 2015. These show that private sector employment rose by 226,000 on the quarter and was up by 554,000 over the year. This more than offset the fall in public sector employment which decreased by 19,000 on the quarter and by 48,000 over the year. Over this period over 6 private sector jobs have been created for every public sector job lost. These series exclude the effects of major reclassifications where large bodies employing large number of people have moved between the public and private sectos.

** Monthly data used (November 2015)

Public sector pay and pensions

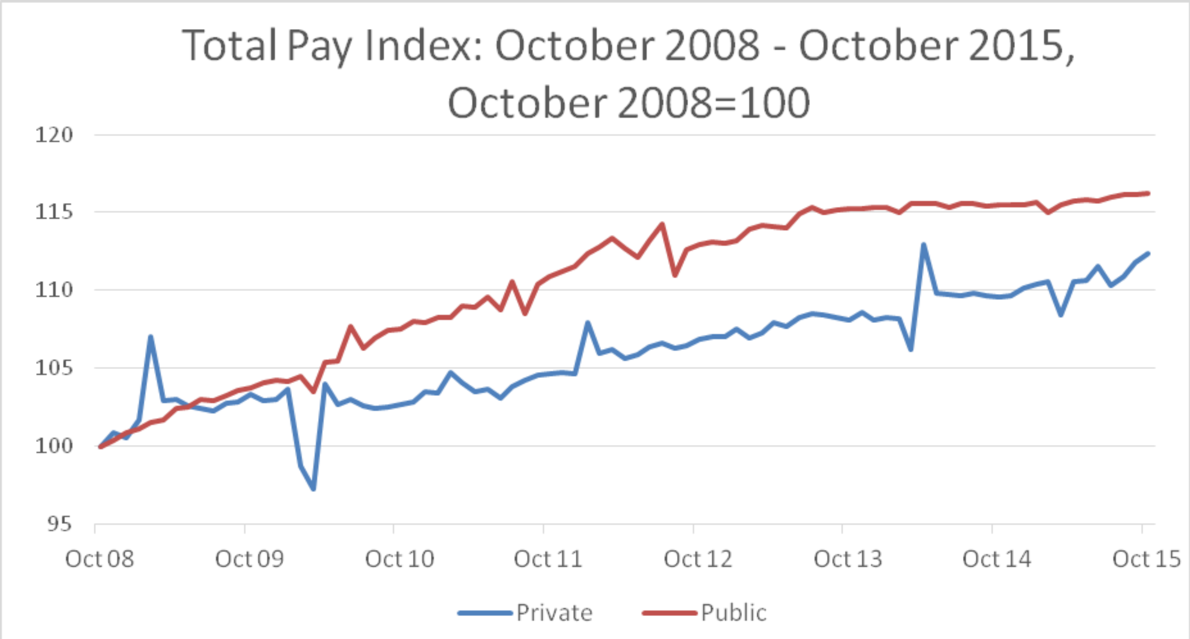
26. The recent recession saw a significant fall in UK wage growth, particularly in the private sector. Analysis by IFS and ONS shows that over the last few years public sector workers have benefitted from a higher pay growth on average compared to workers with similar characteristics in the private sector. While the pay differential between public and private sector workers is narrowing, the overall remuneration of public sector employees when taking employer pension provision into account continues to be above that of the market.

27. Earnings growth in the private sector has been strong throughout 2015 and in the three months to October, total pay growth (including bonuses) stood at 2.7%, while private sector regular pay growth (excluding bonuses) also stood at 2.3%. Although low inflation has helped boost real wages, nominal private sector wage growth remains below rates seen before the recession (about 4-5% per annum).

28. Public sector average earnings growth was 1.3% in the three months to October 2015. Regular earnings (excluding bonuses) also grew by 1.3% over the same period. These rates stood above the rate of inflation in this period (-0.1%) but still below the pre-recession average growth rate, as in the private sector.

29. Historically, public sector wages tend to fall and recover at a slower pace during economic cycles than private sector wages – i.e. there can be a delay between a recession occurring and public sector wage adjustment. Since July 2014, private sector earnings growth has been faster than growth in public sector wages, but this follows on from sustained public sector wage growth in the years immediately following the recession. From the three months to March 2008 to the three months to October 2015, total average private sector earnings have increased by 10.4%, while those in the public sector have increased by 16.1%. The overall level of public sector average weekly wage remains above that of the private sector. Figure 5 compares the growth in average public and private sector weekly earnings since 2008.

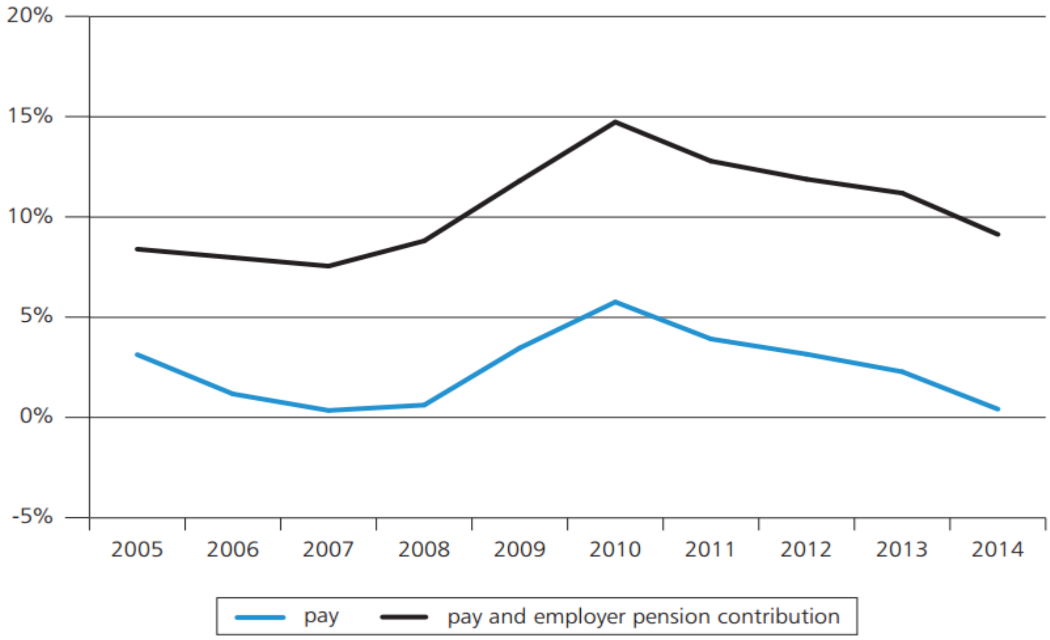
Figure 5: Total pay comparison



Source: Average Weekly Earnings, ONS Labour Market Statistics, December 2015

30. When considering changes to remuneration, it is important to consider other elements of the total reward package. Including hourly employer pension contributions to hourly pay and bonus, recent HMT analysis finds that public sector workers benefit from an 8% premium compared with their private sector counterparts. This is supported by the IFS (October 2014 paper), who found that a 4.6% pay premium continues to exist in favour of public sector workers and that the premium increases significantly if one incorporates pension payments in the analysis. This premium is driven by a number of factors including high pay for women, and protection for the low paid in the public sector. Figure 6 shows the comparison of average hourly earnings for public and private sector workers with similar characteristics across time.

Figure 6: Estimated public-private hourly pay differential



Source: HM Treasury analysis based on Annual Survey of Hours and Earnings data, comparing the average hourly earnings of public and private sector workers with similar characteristics.

31. The government wants to move from a low wage, high tax, high welfare society to a higher wage, lower tax, lower welfare society and wants to do this in a fair way by ensuring that low wage workers take a greater share of the gains from growth. An essential part of this is the introduction of a new National Living Wage (NLW) for workers aged 25 and above.

32. At Summer Budget 2015, it was announced that the NLW will increase pay to £7.20 per hour from April 2016, rising to £9.00 per hour by 2020, benefitting workers across the economy. Estimates indicate that the NLW policy is expected to directly benefit approximately 200,000 public sector jobs.

Pension reforms

33. One major factor in the overall reward package is pension provision. In the last few decades pension provision in the public and private sectors has diverged, in response to pressures around longevity, changes in the business environment and investment risk. This has led to a sharp decrease in the provision of defined benefit schemes in the

private sector. Around 85% of public sector employees are members of employer-sponsored pension schemes, compared to only 35% in the private sector.

34. Following a fundamental review of public service pension provision by the Independent Public Service Pensions Commission, the government has introduced key changes to the pension element of the remuneration package. New public service pension schemes introduced in April 2015:

- calculate pension entitlement using the average earnings of a member over their career, rather than their salary at or near to retirement;
- calculate pension benefits based on Normal Pension Age linked to the member's State Pension Age; and
- include an employer cost cap mechanism, which will ensure that the risks associated with pension provision are shared with scheme members to provide backstop protection for the taxpayer.

35. The changes introduced through the Public Service Pensions Act 2013 will save an estimated £65 billion by 2061-62.

36. Wider changes to public service pension provision have also taken place. Progressive increases in the amount that members contribute towards their public service pension began in April 2012 and were phased in over three years, with the final increases made in April 2014. Members are now contributing an average of 3.2 percentage points more, delivering £2.8 billion of savings a year by 2014-15.

37. Protections from the impact of the contribution changes have been put in place for the lowest paid. Those earning less than £15,000 were not subject to increases; and increases for those earning up to £21,000 (£26,000 for Teachers) were capped at 1.5 percentage points.

38. Public service pensions will remain among the best available and will continue to offer members guaranteed, index-linked benefits in retirement that are protected against inflation. Private sector workers buying benefits in the market would have to contribute over a third of their salary each year to buy an equivalent pension.

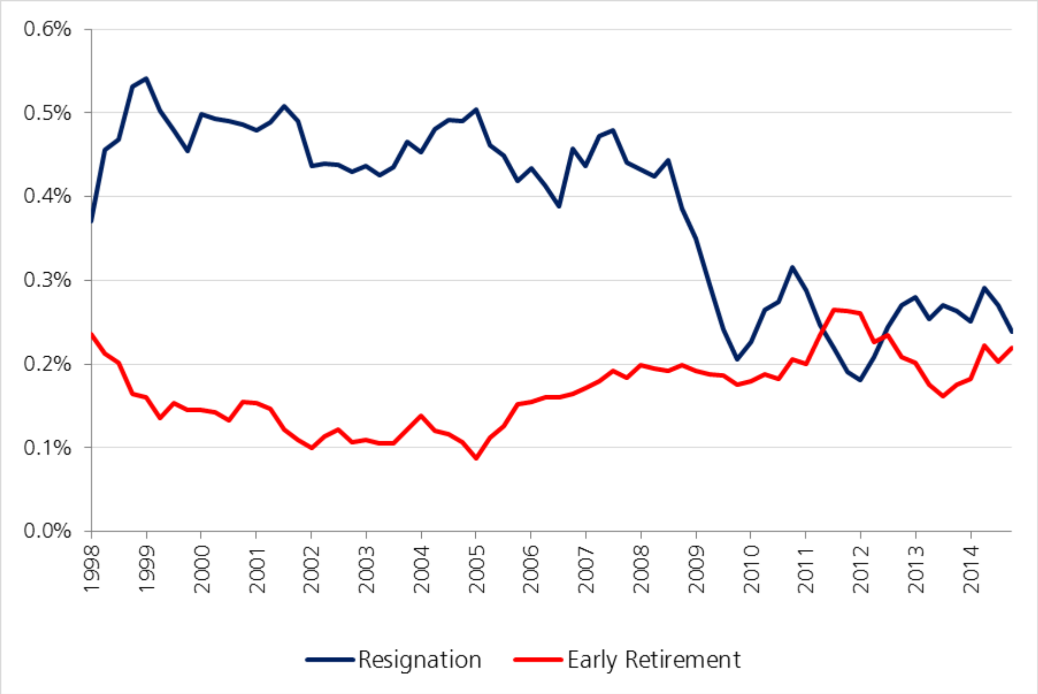
39. Putting together the evidence on pension provision and pay levels – and recognising that there will be significant variation between and within individual workforces – the overall remuneration of public sector employees is above that of the market. The government is therefore clear that any changes to public service pensions, including the progressive increase in contributions from 2012-13, do not justify upward pressure on pay.

Recruitment and Retention

40. Across the whole economy there is evidence that the labour market is performing strongly. There has been strong growth in employment and tightening of labour market slack, a record high number of vacancies. However, there is limited evidence of widespread recruitment and retention issues within the public sector, and resignation rates continue to be below pre-recession levels in this sector. Figure 7 demonstrates recent resignation and early retirement rates in the public sector.

`

Figure 7: Resignation and Early Retirement Rates (up to Q4 2014)



Source: Labour Force Survey Microdata, ONS and HM Treasury analysis

41. The rate at which people are resigning from the public sector remains substantially below pre-recession levels. Within the public sector, the resignation rate was relatively constant prior to the recession, in the region of 0.4 – 0.5%. From the middle of 2008 this rate fell sharply to 0.2 – 0.3%, potentially relating to opportunities outside the public sector becoming scarcer. Since then it has made little sustained recovery and remained within the range up to 2014. The early retirement rate figures increased between 2010 and 2011, but have subsequently fallen back again.

42. The CIPD Labour Monthly Outlook, Autumn 2015, indicates that amongst all private sector firms, where pay has increased by 2% or more, in only 22% of cases were pay awards set at that level because of recruitment and retention issues.

43. There is limited evidence of widespread recruitment and retention issues in the public sector. The government's expectation that the 1% pay award for 2016-17 will be applied in a targeted manner to support the delivery of public services ensures that flexibility exists to meet any recruitment and retention pressures.