

Illustrating the Impact of Increased Social Security Spending on the Scottish Economy

Technical Note

March 2024

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Introduction

The Scottish Government is investing a record £6.3 billion in social security benefits in 2024-25 to support the most vulnerable in our society. This spending provides an important financial safety net to those most in need. In general, social security spending can also have a role in supporting the broader economy, acting as a stabiliser for the economy by providing additional income when there is a downturn. This provides short-term benefits, as supporting those who need it most can increase spending in the economy.

These policies have the potential to improve long-term economic outcomes, by reducing the worst impacts of financial distress. Policies which, for example, support people's health and wellbeing, and so also support their continued participation in the labour market, can have a lasting positive economic impact.

This analysis is supported by the emerging evidence relating to the outcomes associated with social security spending administered by Social Security Scotland.¹ Early analysis shows that social security spending is supporting a variety of Scottish Government outcomes related to reducing child poverty and material deprivation, improving health and wellbeing and helping to narrow inequalities. It also sets out the potential that social security payments have to improve economic outcomes. For example, investment today to mitigate the harmful effects of poverty can lead to longer term benefits to the economy in future through:

- reduced demand for, and expenditure on, public services, such as reducing health-care spending;
- improved productivity, through a healthier, more productive, workforce; and
- greater and more equal labour market participation, by reducing labour market barriers, particularly for disadvantaged groups.

This technical note explores how some of those economic channels can be modelled, with a focus on GDP. In addition to their impact on GDP, all of these channels would also lead to improved tax revenues in future, although these impacts are not considered in this note. This technical note sets out an approach to modelling both short-run impacts and potential longer-term impacts. Further detail of the modelling is in Annex A.

¹ [Examining Outcomes Associated with Social Security Scotland Spending: An Evidence Synthesis](#)

Illustrative Economic Impacts

Short-term

In 2024-25, the Scottish Government will invest a record £6.3 billion in new and devolved social security benefits to support the most vulnerable in our society. This is £1.1 billion more than the UK Government allocation to the Scottish Government for social security as part of the fiscal framework.

We use a fiscal multiplier approach to consider the short-term impacts this additional social security spending could have on Scottish GDP. This is the same methodological approach that the Office for Budget Responsibility (OBR) use in their short-term demand side analysis of UK Government policy changes.

For example, as can be seen in Table 1, the OBR estimate that the short-term economic impact of increasing spending on areas of Annual Managed Expenditure (AME), which includes most social security spend at the UK Government level, tends to have a higher short-term economic impact relative to changes to resource spending (RDEL), or tax.

Table 1: Fiscal multipliers published by the Office for Budget Responsibility

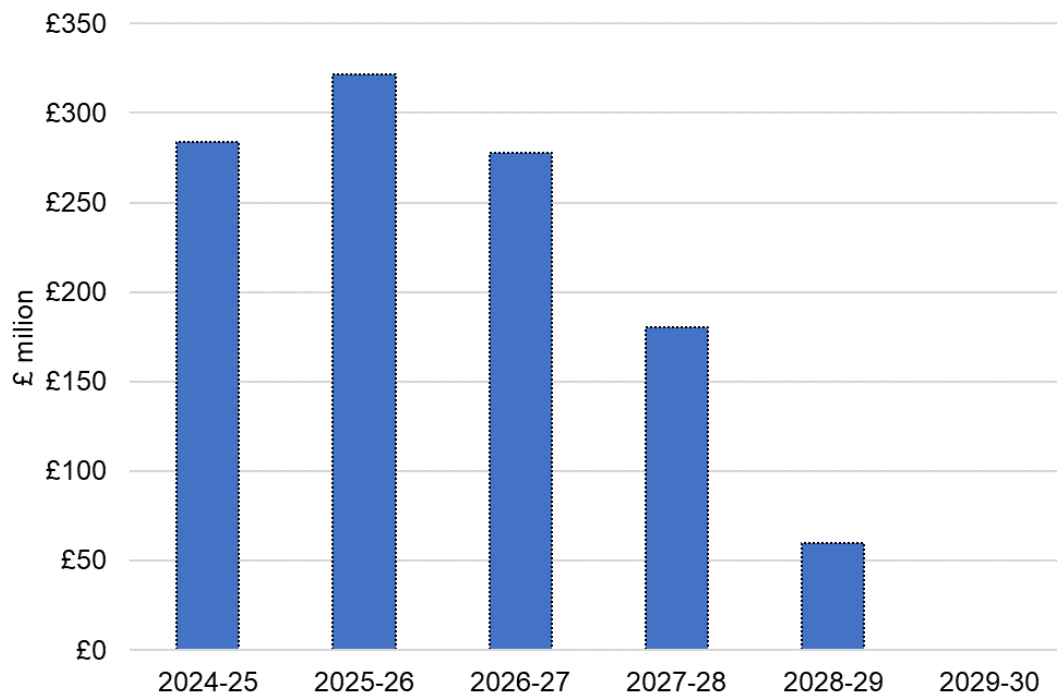
	Impact of a one per cent of GDP increase in category on real GDP					
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
Tax	0.33	0.30	0.23	0.14	0.05	0.00
RDEL	0.34	0.31	0.22	0.10	0.03	0.00
CDEL	1.00	0.83	0.43	0.23	0.07	0.00
CJRS	0.15	0.14	0.11	0.06	0.02	0.00
Other AME	0.60	0.57	0.43	0.23	0.07	0.00

Source: Office for Budget Responsibility: Economic and Fiscal Outlook, November 2020, Box 2.1

Applying these multipliers suggests that the additional £1.1 billion of social security spending could result in a £300 million boost to Scottish GDP in the short term (in 2024-25 prices).

As can be seen in Figure 1, this impact is primarily focused on the short-term. The economic impact fades over time as the policies cause prices in the economy to adapt, such as the level of inflation or wages, which then results in a tapering of the economic impact back to zero over time.

Figure 1: Short-term fiscal multiplier analysis – Net impact on the size of the economy from additional spend on social security



Source: SG Analysis using Office for Budget Responsibility (OBR) fiscal multipliers

Long-term

As well as short-term impacts, social security spend can help deliver long-term improvements to the Scottish economy, through delivering positive supply-side improvements in the labour market. Through supporting people into the labour market and to find good, well paid, rewarding jobs, such programmes can help provide lasting change.

Scottish Government labour market and housing policies are expected to support more people into employment, while social security, childcare and labour market policies have the potential to reduce barriers to participation, particularly for disadvantaged groups.

Relatively small increases in participation can have positive impacts on economic performance. **Illustrative modelling suggests that if we can increase labour force participation by around 0.25 percentage points this could boost GDP by around £180 million a year over the long-term (in 2024-25 prices).** This underlines the importance of measures that increase labour market participation.

Discussion

Whilst the analysis in this note has identified the potential for social security spending to have positive economic impacts in both the short and longer term, it has a number of limitations that should be borne in mind. Our approach does not consider the long term impact of policy changes on competitiveness, for example through changes to labour market incentives. It also does not consider the returns of alternative policies, such as infrastructure investment, which would have different demand and supply impacts. Our analysis focuses on modelling the impacts of additional spending aimed at reducing poverty and inequality.

As noted above, the fiscal multipliers analysis relies upon the assumption that the social security received is more likely to be spent than saved. This is supported by the latest evidence relating to the new social security programmes. The interim evaluation of the Scottish Child Payment² shows that the payment has generally allowed parents and carers to spend money that they otherwise would not have spent. Additionally, the evaluation shows that recipients tended to spend the whole payment, with only a small number saying they tried to save some of the money. This suggests a higher than average propensity to consume, meaning that these households spend more and save less of their income.

Given that Social Security multipliers are estimated to be larger than those for other types of resource spending in the short term, particularly during an economic downturn, this type of spend can help stabilise the economy. This means that such spending does not just increase the income of affected households but can also provide short-term support to growth through an increase in aggregate expenditure.

In the longer term, sustained growth requires improvements in participation or productivity. Therefore it is important to complement spending on social security with policies which improve the supply-side of the Scottish economy.

² [Scottish Child Payment: interim evaluation - gov.scot \(www.gov.scot\)](http://www.gov.scot)

Annex A – Modelling Assumptions

Short-term

We have used a fiscal multipliers approach to measure the impact of social security policies on the Scottish economy. Fiscal multipliers measure the short-term impact of discretionary fiscal policy on output. They are usually defined as the ratio of a change in output to an exogenous change in fiscal policy. This approach is used by a range of bodies that draw heavily on a range of academic research around this topic.

The additional social security spending is estimated as the difference between total Scottish Government social security spending and the social security block grant adjustment, as set out in the latest Scottish Fiscal Commission forecasts.³ As shown in the table below, this is around £1.1 billion in 2024-25, rising to £1.5 billion in 2028-29.

Table A.1: Estimated additional social security spending in Scotland

	2024-25	2025-26	2026-27	2027-28	2028-29
Total social security spending	6,283	6,861	7,253	7,616	7,999
Social security BGA	5,191	5,625	5,931	6,231	6,497
Additional social security spending	1,092	1,236	1,322	1,385	1,502

To translate this into an impact on the economy, we apply fiscal multipliers used by the OBR, which are shown in the table below. There is obviously a range of uncertainty around these estimates. The OBR note that their fiscal multipliers have been drawn from the empirical literature. The OBR review their multipliers periodically, with the latest multipliers published as part of their November 2020 Economic and Fiscal Outlook.⁴

Table A.2: Estimated additional social security spending in Scotland

	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30
Tax	0.33	0.3	0.23	0.14	0.05	0
RDEL	0.34	0.31	0.22	0.10	0.03	0
Other AME	0.60	0.57	0.43	0.23	0.07	0

The analysis assumes that the increase in social security is not funded by borrowing, reflecting the Scottish Government's powers. This means that any additional social security spending would have to be financed by either increased taxation or reprioritising spending within the Scottish Government budget. We consider both approaches below.

We assume that the tax multiplier is a reasonable approximation for Scottish tax changes, that the RDEL multiplier is a reasonable approximation for Scottish resource spend, and that Other AME, which is primarily welfare expenditure, is a reasonable approximation for Scottish social security spending. The changes are

³ [Scotland's Economic and Fiscal Forecasts – December 2023 – Scottish Fiscal Commission](#)

⁴ [Economic and fiscal outlook - November 2020 \(obr.uk\)](#) page 32, Table A

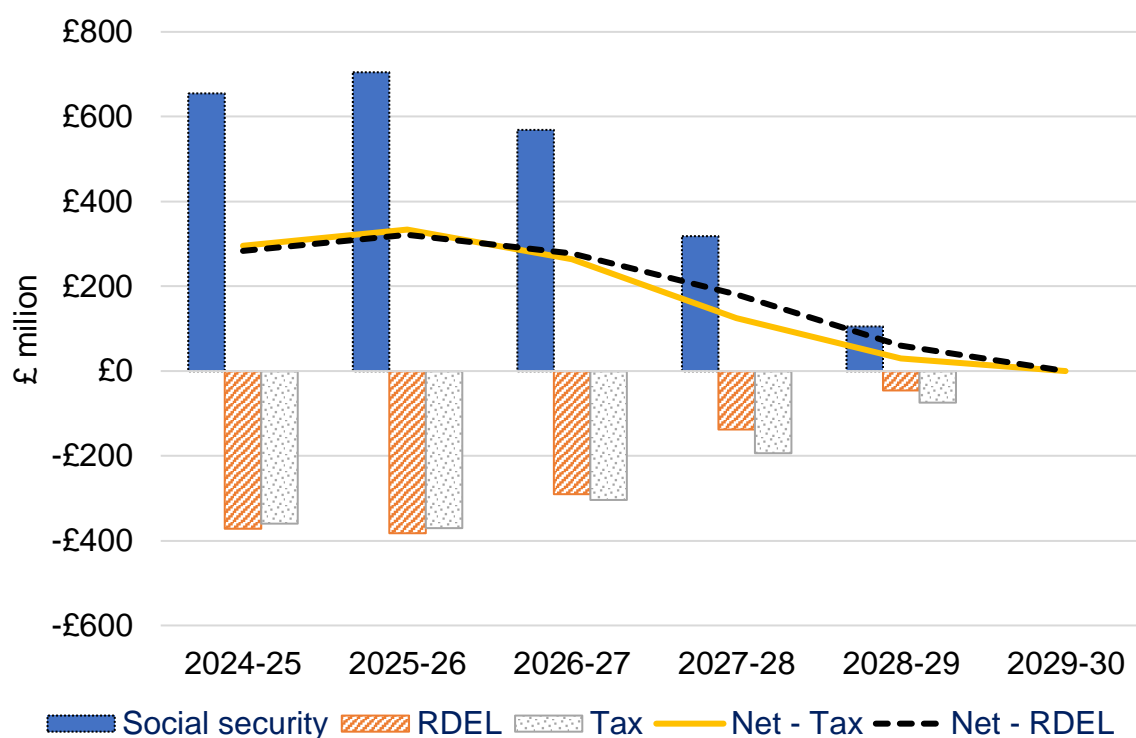
expressed as a share of GDP using the Scottish Fiscal Commission’s December 2023 Economic and Fiscal Forecasts, and the multipliers are applied to these. The resulting impact on GDP is shown in the table below.

Table A.3: Net impact of additional social security spending on Scottish GDP (£ million)

Source of finance	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30
Tax	£295	£334	£264	£125	£30	£0
RDEL	£284	£321	£278	£180	£60	£0

This shows that the source of funding has a relatively minor impact on the results. In both cases, the additional social security provides a short-term impact averaging around £300 million from 2024-25 to 2026-27. Figure A.1 below shows separately the positive impacts of increasing social security spending, the partially offsetting impacts of funding this by either taxation or resource spending, and the net effect.

Figure A.1: Multiplier effects from spend on social security (AME), and the offsetting from either taxes or resource spending (RDEL)



Source: SG Analysis using Office for Budget Responsibility (OBR) fiscal multipliers

Long-term modelling

We have used the Scottish Government's Global Econometric Model (SGGEM) to perform an illustrative scenario analysis on how a change in labour market participation could impact the Scottish economy.

SGGEM is an economic model that was commissioned from the National Institute of Economic and Social Research (NIESR) and one of its strengths is that it is a modified version (splitting the UK into Scotland and the rUK) of NIESR's own Global Macroeconomic Model NiGEM,⁵ which is an internationally recognised and scrutinised macroeconomic model which has been used by institutions such as the OECD, European Central Bank and the Bank of England. Consequently, the model is a well-developed general equilibrium model that is well suited to examining the macro-economic impact of various scenarios, including changes in the labour market.

An illustrative shock is calibrated to the model to increase the participation rate of individuals aged 16+ in Scotland by 0.25 percentage points. As this is an illustrative scenario analysis, no other assumptions or shocks are applied. It is assumed that fiscal policy and monetary policy in the model remain endogenous – in other words, they will react and adapt to the effects of the change. However, given the size of the shock is relatively small it does not have a significant effect. Additional sensitivity scenarios were run where monetary Policy and fiscal Policy are held exogenous and it does not materially alter the results.

The illustrative modelling suggests that permanently raising the participation rate by 0.25 percentage points could result in the overall size of the economy being around 0.1 per cent higher over the long-term. This would be equivalent to around £170 million in 2022 prices based on the latest published National Accounts, or alternatively around £180 million in 2024-25 prices using recent GDP forecasts.

Office of the Chief Economic Adviser

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⁵ Further information on the model can be found [here](#).



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