

Why we need public spending



(20 May 2014) **New EPSU/PSI Study launched today at EPSU Congress, by Dave Hall, PSIRU**

Introduction and Executive summary

This paper aims to explain why public spending, in particular on public services, is economically and socially vital. It is not an economic liability – rising public spending has been part of economic growth for over 100 years; it supports half the formal employment in the world, much of it in the private sector; it delivers services like healthcare and public goods like renewable energy more efficiently and effectively than the private sector; it is a vital way of creating greater equality, not only through benefits but through public services; extra spending can be financed easily in all countries by taxing the rich, eliminating corporate tax evasion, and property taxes; government deficits are far more efficient than PPPs or privatisation.

Austerity policies are being applied in many countries. Government spending and

deficits are identified as key economic problems. But government deficits are the result of the crisis, not a cause of it. The austerity policies damage the prospects for economic growth, rather than improving them. They are being implemented as a way of reducing the role of public services, public employment and public spending. Far from being a burden on the economy, public spending has had a consistent positive effect for over a century. This positive link works in developing countries as well as high income countries. Public spending supports economic growth through investment in infrastructure, through supporting an educated and healthy workforce, through redistributing income to increase the spending power of poorer consumers, providing insurance against risks, providing direct support for industry, including through technological innovation, and increasing efficiency by taking on these functions.

Public spending supports employment, in both high income and developing countries, through: direct employment of public service workers; indirect employment of workers, by contractors supplying outsourced goods and services; employment of workers on infrastructure projects; extra demand and jobs from the spending of the wages of these workers and also of recipients of social security benefits (the 'multiplier effect'); the combined effect of these mechanisms is to support half the formal jobs in the world; subsidies to support employment by private companies, or by providing employment guarantees; providing formal jobs with decent pay and conditions; government procurement is used to require 'fair wages' from private contractors, to reduce gender and ethnic discrimination, and strengthen formal employment of local workers. The purpose of public spending and public services is to achieve public objectives.

These objectives include, for example, ensuring universal education and universal access to healthcare; environmental objectives such as the reduction of greenhouse gas emissions and management of waste; and economic objectives such as full employment. In a wide range of areas, these objectives are most effectively and efficiently achieved through public spending and public services. This section examines three policy areas where public spending and public services are key – healthcare; housing; and climate change. The growth of profits at the expense of income from wages, and the rise in the incomes of the richest households, have created large and growing inequalities, with damaging economic and social effects. Along with trade unions, public spending and public services are the most powerful engines of greater equality.

Public spending redistributes money income through social security benefits, but public services make an even greater contribution to equality. The value of public services is equally distributed, and in OECD countries this is equivalent to an extra 76% of the disposable cash income of the poorest 20%. In Latin America, public services have the same effect, making a greater impact on equality than social security benefits. In Asian countries too, the benefits of public healthcare and education are powerful equalising mechanisms. Infrastructure for electricity, water and other services not only increases access for all, but improves employment opportunities, especially for women. And through employing more people on better pay and conditions, public services also improve income equality. Government revenues consist of taxes of various kinds and income from other sources. Countries with higher GDP have higher levels of taxation, so an increasing level of taxation is a key part of economic development.

The total amount needs to be sufficient to pay for spending on public services and social security, and the burden of taxation should be fairly distributed. But neoliberal policies have attempted to reduce taxation, and have shifted the tax burden away from the rich, and corporate profits, on to ordinary people. All countries could increase their revenues substantially, just by increasing taxes on high incomes, property and corporate profits. This requires action to strengthen tax collection systems, and to deal with tax avoidance and the use of tax havens. The supporters of austerity programmes argue that government debt damages economic growth, but there is no evidence to support this – a Harvard University paper which claimed to find a connection has been discredited. Government borrowing is a key economic instrument for driving economic activity, and is much

cheaper than borrowing by private companies, which have to pay much higher interest rates. Privatisation and PPPs are unnecessary, costly and damaging ways of raising money.

Changing current policies depends on political activity. Market mechanisms do not deliver the level of public services which countries need. The decisions which drive the development of public spending, or the imposition of austerity, are the outcome of political processes at national and international level.

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