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Scottish Budget 2021-22

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This briefing summarises the Scottish Government's spending and tax plans for 2021-22. More detailed presentation of the budget figures can be found in our Budget spreadsheets. Infographics created by Andrew Aiton, Kayleigh Finnigan and Laura Gilman.

SCOTTISH BUDGET:
2021-22

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Executive Summary

This year's Scottish Budget is being published later than normal and in advance of the UK Government's Budget scheduled for March. The later than normal publication has implications for the time available for parliamentary scrutiny of the Scottish Government's proposals. Preceding the UK Government's Budget also means that the total Scottish spending envelope for 2021-22 is still uncertain, although it is more likely to go up than down.

The terrible toll that COVID-19 has taken on the country is reflected in the Scottish Fiscal Commission's (SFC) economic forecasts, which suggest that Scottish economic output fell dramatically in 2020 and is only likely to return to pre-pandemic levels in 2024.

A Fiscal Framework defined Scotland-specific economic shock is triggered for the first time, meaning that the Scottish Government has greater fiscal flexibilities available to it for the next three financial years. However, the triggering of this Fiscal Framework clause is more likely to be down to forecast timing issues rather than the Scottish economy being negatively out of kilter with the UK as a whole.

The inflation measures that would normally be used to calculate “real terms” changes have been impacted by the pandemic. This means that “real terms” inflation adjusted numbers look a little skewed. We have therefore opted to present the Budget numbers in this year's briefing in “cash terms” (i.e. unadjusted for inflation). Using a GDP deflator which is averaged over the two years of the pandemic, rather than using the unadjusted GDP deflator, suggests a different profile of real terms changes.

Scottish spending power will be boosted in 2021-22 by borrowings totalling £769 million, a Scotland Reserve drawdown of £431 million and an assumption of £500 million more in COVID-related Barnett consequentials from the UK Government. Resource spending on day-to-day activities will increase by 11.2% next year (an increase which includes planned COVID-19 spending), however, there will be a slight fall of 0.7% in Capital (infrastructure) spending.

Health remains the most significant budgetary priority of the Scottish Government. Even before taking account of additional COVID-19 spending, the health budget is increasing by 5%. On top of this, the Scottish Government currently plans to allocate a further £869 million to the health budget for COVID-19 funding in 2021-22. With these increases, the health budget will account for 43% of all day-to-day spend next year.

In recent years, the allocation to local government has been one of the main issues of controversy during parliamentary consideration of the budget. The combined Budget document figure for General Resource Grant (GRG) and Non-Domestic Rates Income (NDRI) only (i.e. the amount of money to deliver services over which local authorities have control) increases by 1.9% in cash terms, or £186 million. Once specific, ring fenced resource grants are included, then the combined figure for the resource budget increases by 2.5% in cash terms, or by £252 million. The total capital budget sees a decrease in cash terms this year, of -20.7% or by £161 million, though this is mostly driven by a decrease in non-recurrent specific capital grants.

The Scottish Government proposes to retain the same five-band income tax structure that has been in place since 2018-19. With the exception of the top rate threshold, which remains at £150,000, all other thresholds are increased in line with inflation in the Scottish

Government's proposals.

The proposed income tax policy for 2021-22 means that all taxpayers will pay less income tax next year. However, the differences are very small – only around £14 over the year for those on incomes below £25,000, rising to just over £60 per year for those earning more than £44,000. Much of this change comes from the UK Government's plans to increase the personal allowance to £12,570, rather than the Scottish Government's proposed changes.

Assuming no further changes to UK income tax at the UK budget in March, Scottish taxpayers earning less than around £27,000 will pay just under £21 less income tax in the year than they would in the rest of the UK. This accounts for 54% of all Scottish taxpayers. However, those earning more than £50,000 will be paying at least £1,500 more income tax per year than they would in the rest of the UK.

One hundred per cent business rates relief for retail, hospitality and leisure businesses was due to be in place until 31 March 2021. As part of the Budget statement, the Cabinet Secretary announced (noting that the UK Government had not yet announced an extension) that this would be extended for a further three months, and potentially further should the UK Government take similar action.

In addition to this relief extension, the Cabinet Secretary announced that the poundage rate for Non-Domestic Rates would be reduced by 0.8p to 49p, making it the lowest poundage rate in the UK.

Ninety million pounds is provided in the Budget to allow local authorities to freeze Council Tax (this figure is equivalent to a 3% increase).

SFC forecasts for Income Tax and fully devolved taxes are £539 million more than the provisional block grant adjustment (BGA) that has been applied. This means that the Budget is £539 million better off than it would be without tax devolution. However, this is based on current forecasts which are likely to be revised, leading to reconciliations further down the line.

The 2021-22 BGA addition to the Scottish Budget for Social Security is £3,310 million. However, the Social Security spend in the next year is forecast by the SFC as being over £300 million higher, at £3,614 million. This is partly due to introduction of new benefits specific to Scotland, such as the Scottish Child Payment.

The SFC acknowledge a materially different pathway of COVID-19 and restrictions relative to their assumptions would mean the pathway of the economy, taxes and social security spending could be significantly different from their forecasts.

On public sector pay, the Scottish Government has opted not to replicate the UK Government's pay freeze. The Budget proposes an increase of 1% for public sector workers earning below £80,000 and a limit of £800 increase for those earning above £80,000. For lower paid staff, the Budget proposes a continuing requirement for employers to pay the real Living Wage of £9.50 per hour and provides for a guaranteed cash increase of £750 for all staff earning less than £25,000.

A number of other documents were published alongside the Budget including the Medium Term Financial Strategy, the Equality and Fairer Scotland Budget Statement and a Carbon Assessment. These are all analysed in this briefing.

Judging by initial comments made by opposition parties in the Chamber, it is likely that the proposals in the Budget will need to change in order to command the majority support of MSPs required to pass.

Context for Budget 2021-22

Scottish Budget 2021-22 [1] was published on 28 January 2021 and presents the Scottish Government's proposed spending and tax plans for 2021-22. The publication marks the start of an intensive period of parliamentary scrutiny and political negotiation as the Government seeks majority MSP support for its tax proposals and Budget Bill in advance of the new financial year.

The Budget incorporates devolved tax forecasts undertaken by the Scottish Fiscal Commission (SFC). As well as producing point estimates for each of the devolved taxes (including non-domestic rates income (NDRI)) for the next five years, the SFC is also tasked with producing forecasts for Scottish economic growth and spending forecasts for devolved social security areas. The SFC's forecasts can be found in Scotland's Economic and Fiscal Forecasts [2] .

This Budget comes against the backdrop of a global pandemic that has impacted the health and fabric of countries across the world. Scotland and the world has been changed completely by the events of this year and this Budget and economic forecasts reflect that. The end of the Brexit transition period on 31 December 2020, which would normally dominate news and Government statements, also feeds into the SFC's forecasts.

The SFC's judgement is that Scottish economic output will fall by 10.7% in 2020, before increasing by 1.8% in 2021, 7.5% in 2022, 1.6% in 2023 and 1.6% in 2024. Such has been the impact of the pandemic, the SFC estimate that Scotland won't return to pre-pandemic levels of economic output until 2024.

Table 1: SFC Scottish GDP forecasts

	2020	2021	2022	2023	2024
Scottish Fiscal Commission	-10.7%	1.8%	7.5%	1.6%	1.6%

A Scotland-specific economic shock

Like the SFC for Scotland, the Office for Budget Responsibility (OBR) is mandated to produce economic forecasts for the UK. These were last produced in November 2020 and new OBR forecasts for the UK will be available in March alongside the UK Budget.

The OBR and the SFC have both stated that the COVID-related Scottish and UK economic impacts are broadly in line with each other. However, the timing of the OBR forecasts in November (prior to the new COVID-19 variant and subsequent lockdown) means that OBR forecasts were more optimistic then than the SFC's are now. It is likely that the OBR forecasts to be published alongside the UK Budget on 3 March will be more pessimistic.

Meanwhile, the forecast divergence in Scottish and UK growth means that the Fiscal Framework conditions for the triggering of a Scotland-specific economic shock are met for the first time, namely:

- Annual GDP growth in Scotland, on a four-quarters-on-four-quarters basis is below 1%.

- Four-quarters-on-four-quarters growth in Scotland is 1.0 percentage point or more below the UK.

This forecast timing difference – and the resulting triggering of a "Scotland-specific shock" – has the effect of increasing the fiscal flexibilities available to the Scottish budget. Specifically, the resource borrowing limit increases from £300 million to £600 million for the next three financial years. However, this can only be used to address forecast errors. In addition, the annual drawdown limits from the Scotland Reserve are removed for the same three-year period. This means that rather than an annual limit of £250 million resource and £100 million capital, the Scottish Government can draw down up to the Reserve's maximum limit of £700 million.

Even if revised forecasts or outturn data show that the conditions for a Scotland-specific shock were not met, the fiscal flexibilities will not be revoked. So, these flexibilities will be in place until 2023-24.

It is somewhat ironic that the Cabinet Secretary has been calling on the UK Treasury to increase flexibilities for some time. This disconnect in the timing of the OBR and SFC forecasts is likely not how either government intended additional flexibilities to be delivered, but is yet another consequence of the "unprecedented times" that we live in.

It also raises interesting questions which the Fiscal Framework review may wish to ponder, around the timing of UK and Scottish forecasts and how that can have a material impact on the size of the Scottish budget.

COVID-19 in the Budget

Over the course of 2020-21, the Scottish Government received an additional £8.6 billion on top of the original block grant for that year, as a result of the pandemic response. Whenever the UK government spent additional sums in areas of devolved responsibility on its COVID-19 response, the Scottish Government was allocated additional resources via the Barnett formula. During the course of the year, and in response to Scottish Government calls for greater certainty to assist in planning, the UK government agreed to provide a guaranteed amount, rather than allocating additional sums on a piecemeal basis. This guaranteed amount itself increased on a number of occasions and – at the time of the Budget – stood at £8.6 billion.

However, this £8.6 billion is not included in the figures for 2020-21 that are presented in the budget document. Rather, the 2020-21 figures in the budget document are those agreed in February 2020 at the time of the Scottish Budget, prior to the onset of the pandemic. The presentation of baseline figures agreed during the budget process is the normal approach taken by the Scottish Government in its budget presentation. However, for some spending areas (such as health), this means that the 2020-21 baseline figures significantly understate the final budgets. Taking health as an example, additional COVID-19 Barnett allocations have added around £3 billion to the budget.

By contrast, the 2021-22 budget figures do include some planned COVID-19 allocations. The UK Spending Review of November 2020 [3] confirmed plans for an additional £1.3 billion for Scotland in 2021-22 in relation to COVID-19 spending. But the UK Spending Review also highlighted that the UK Government was setting aside £21 billion in contingency funding in recognition of the fact that the "trajectory of the pandemic remains uncertain" and to "allow the necessary support to be put in place and adapted through the course of next year".

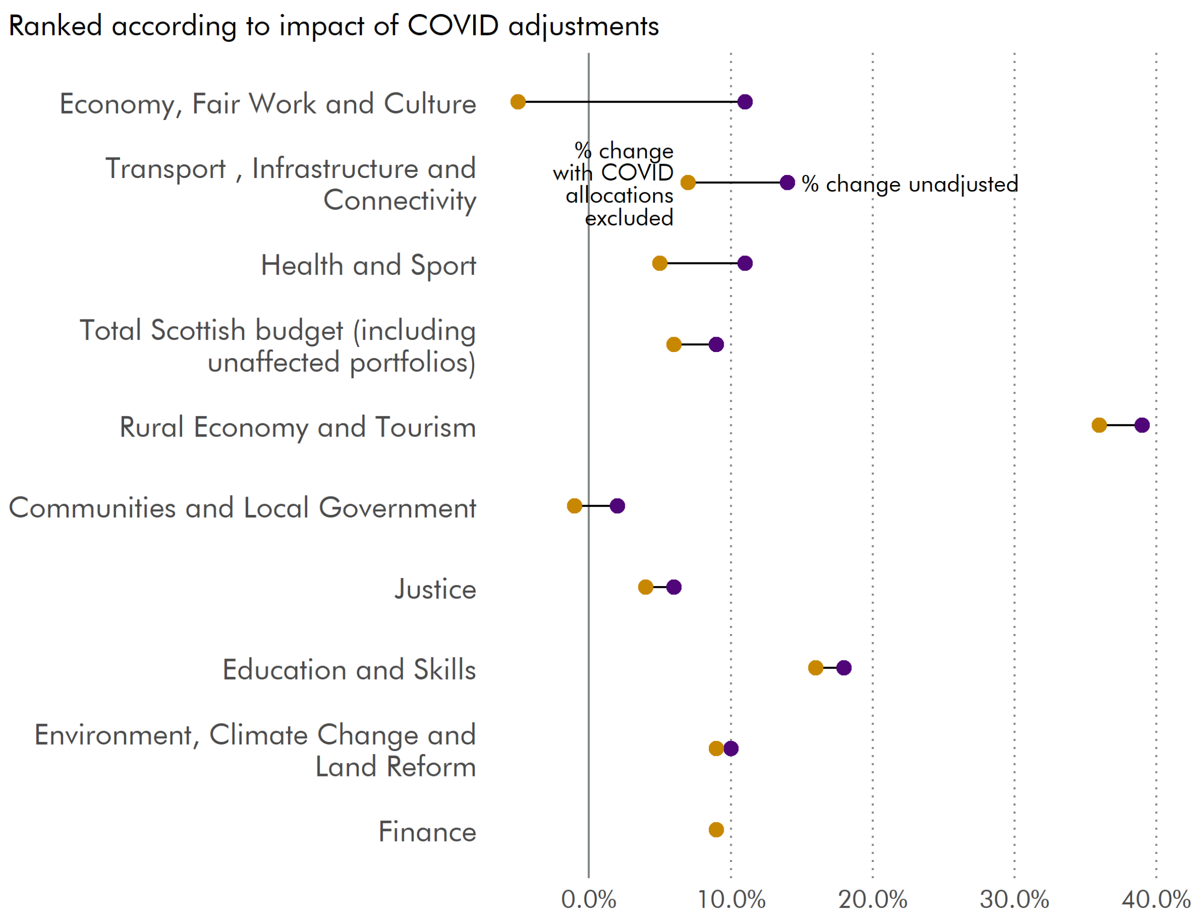
This raises the strong possibility of further COVID-19 related expenditure in 2021-22, and resulting Barnett consequentials for Scotland. In view of this, the Scottish Government decided to plan on an additional £500 million of COVID-related Barnetts in 2021-22 and has already allocated these to spending areas, along with the £1.3 billion already confirmed. A significant proportion (£869 million) has been allocated to health. Allocations for other portfolios are shown in Table 2.

Table 2: COVID-19 allocations by portfolio, 2021-22

Portfolio	£m
Health and Sport	869
Communities and Local Government	399
Finance	15
Education and Skills	68
Justice	72
Transport, Infrastructure and Connectivity	230
Environment, Climate Change and Land Reform	3
Rural Economy and Tourism	25
Economy, Fair Work and Culture	147
Total	**1,828**

This approach means that year-on-year comparisons could be misleading for those areas where COVID-19 allocations have been built in to the 2021-22 budgets, as this compares a year with COVID allocations to a baseline without COVID allocations. Figure 1 shows how the budget changes for each portfolio area are affected if 2021-22 COVID-19 allocations are stripped out.

Figure 1: Budget changes before and after adjusting for COVID-19 allocations



Source: Scottish Budget 2021-22

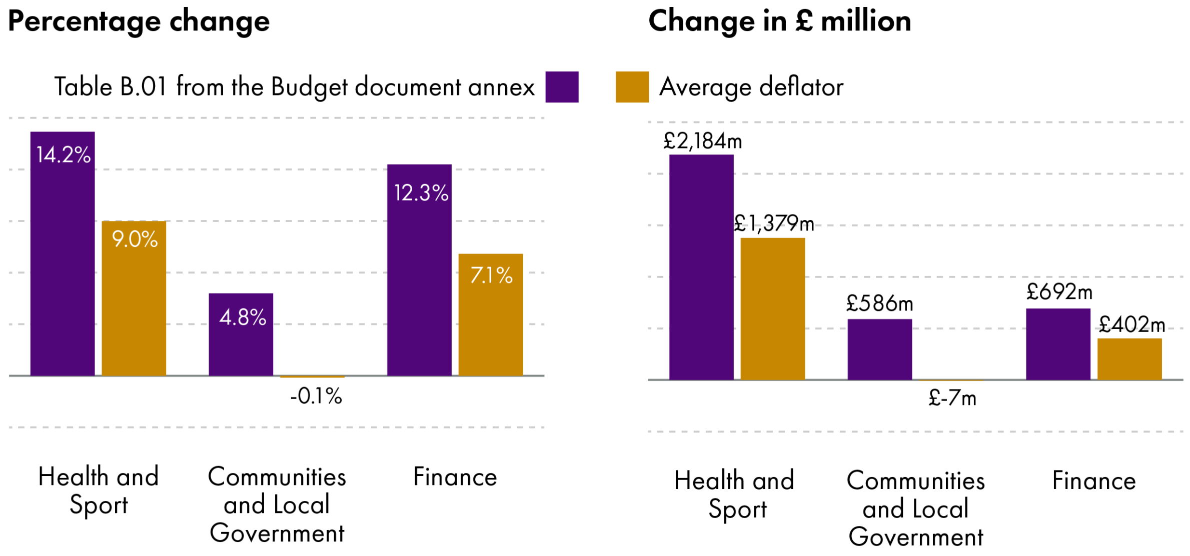
For example, for the Health and Sport portfolio, a direct comparison of the budget figures shows an 11% cash increase in the budget between 2020-21 and 2021-22. However, if the known COVID-19 allocations for 2021-22 are stripped out, the increase is a more modest (although still generous) increase of 5%. For two portfolio areas (Communities and Local Government and Economy, Fair Work and Culture), the cash increases shown by the published budget figures are cash decreases after adjusting for the effect of COVID-19 allocations in 2021-22. For the Scottish budget as a whole, the increase before adjusting for COVID-19 allocations is 9%, but this reduces to 6% after adjusting for COVID-19 allocations.

Measuring inflation

The GDP deflator is a measure of general price inflation in the domestic economy. HM Treasury produce the GDP deflator using data from the Office of National Statistics (ONS).

The ONS produce two different measures of GDP; current prices and constant prices. The ratio of these two different measures is the movement in prices over time. By combining measures of hundreds of different deflators, the GDP deflator can give a broad measure of inflation across the economy. This is used to calculate the real terms change in public spending. COVID-19 has had a significant impact on measurements of Government consumption, which has in turn meant that the forecasts for the GDP deflator in 2020-21 and 2021-22 look a little odd. We discussed these forecasts and the impact they might have on the analysis of the Scottish Budget in a recent blog [4] .

Figure 2: Comparison of real terms change for selected portfolios using an average deflator and the data in table B.01 of the budget document



Source: Scottish Budget 2021-22

In short, the issue is that with any comparisons that include the real terms change in either 2020-21 or 2021-22, but not both, the real terms calculation is being skewed by either the large positive 2020-21 deflator or the negative 2021-22 deflator.

What this means for the analysis of the Scottish Budget is that if you simply calculate the real terms change between 2020-21 and 2021-22, you are using only the negative 2.8 per cent deflator. This means that a cash terms cut can actually be described as a real term increase. The GDP deflator is normally used as it is considered the best measurement of general inflation across the economy, and therefore the most appropriate measure of changes in purchasing power for Government spending. However clearly this is not the case for the years 2020-21-20 to 2021-22 – very few portfolios will have experienced an inflation rate of 6.8% last year or -2.8% this year.

The Scottish Government discuss this in the Budget document, noting that:

> “ Real Terms calculations use the GDP deflator as published by the UK Government at the Spending Review on 25 November 2020 as the measure of inflation within the economy. The GDP deflator as published reflects some volatility as a result of the impact of the COVID-19 pandemic - the figure for 2020-21 is significantly higher than the historic trend and the figure for 2021-22 is negative. As was the case in the UK Spending Review, to smooth the distortion of this anomalous impact an average annual uplift in core funding between 2019-20 and 2021-22 has been presented using the GDP deflators shown below.”

An alternative way of presenting these figures could use the average value of the deflator over these two years. Table 3 sets this out below for the three largest portfolios, comparing a real terms difference using an average deflator with the real terms change as presented in Table B.01 of the Budget document.

Table 3: comparison of 2021-22 real terms calculations

Portfolio	Real terms difference in B.01 £ million	Real terms % change in B.01	Real terms difference using average deflator £ million	Real terms % change with average deflator
Health and Sport	2,184	14.2%	1,379	9.0%
Communities and Local Government	586	4.8%	-7.0	-0.1%
Finance	692	12.3%	402	7.1%

Using the same ‘Communities and Local Government’ TME cash terms figures from Table B.01, instead of a 4.8% real terms increase, we would describe a -0.1% real terms decrease in the 2021-22 Budget.

This method of recalculating the real terms changes in portfolio spending using an average deflator in general does not change the trend in spending. Other than the ‘Communities and Local Government’ portfolio, all portfolios increase in real terms whether calculating using the OBR and Treasury forecast, or using an average deflator. And the calculated real terms decrease in funding for ‘Communities and Local Government’ is just £7 million, only 0.1%.

Using an average measure of inflation over the period does remove the distortion caused by using just one of the particularly volatile years in the comparison, however in our analysis we have decided to use the cash terms figures when calculating changes in spending, as introducing an alternative real terms calculation is likely to cause confusion. Members should be cautious when making any real terms comparisons, particularly if only looking at the change in this year’s spending plans, to avoid possible confusion about the true scale of any increase.

Overall spending

The Budget document presents HM Treasury's Budget Control Limits for the Scottish Budget 2021-22 and two previous years in cash terms. This will grow by 9% in 2021-22.

However, the amounts that will actually be spent next year are higher due to a number of changes agreed between the Scottish and UK Governments. These are set out in the annex Table A.06 of the Budget document, and include technical changes like non-cash items and machinery of government changes.

Key discretionary choices that have been taken by the Scottish Government to boost 2021-22 spending power are the drawing down of the following:

- Reserve monies (£431 million)
- Resource borrowing (£319 million)
- Capital Borrowing (£450 million).

Additionally, on top of the £1.3 billion in COVID consequentials already earmarked for next year, the Cabinet Secretary opted to assume an additional £500 million COVID consequentials as “baked into” her plans. Given there is a £21 billion COVID contingency sitting at the UK Treasury, this appears to be a prudent step.

In terms of what is actually being allocated overall in the Budget (presented in the Annex of the document), the Resource budget (or day-to-day spend) is projected to increase by 11.2% next year, and total just under £38 billion.

Spend on Capital, however, is expected to decrease by 0.7% in 2021-22 and total £5.8 billion.

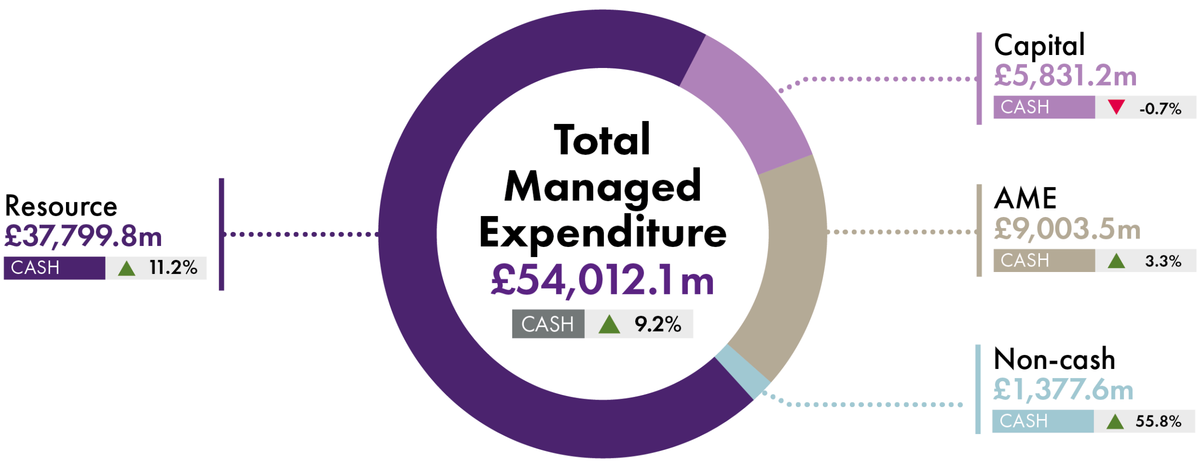
Budget allocations

Total allocations

Total Managed Expenditure (TME) comprises Fiscal Resource, non-cash Resource, Capital and Annually Managed Expenditure (AME). TME in 2021-22 is £54,012 million. Figure 3 shows how this is allocated. As explained above, these figures differ to the HM Treasury Budget Control limits.

Fiscal Resource (which covers day-to-day expenditure) and Capital (covering infrastructure expenditure) are the elements of the budget over which the Scottish Government has discretion. AME is expenditure which is difficult to predict precisely, but where there is a commitment to spend or pay a charge, for example, pensions for public sector employees. Pensions in AME are fully funded by HM Treasury, so do not impact on the Scottish Government's spending power. Non-Domestic Rates are also classed as an AME item in the budget and form part of local government spending.

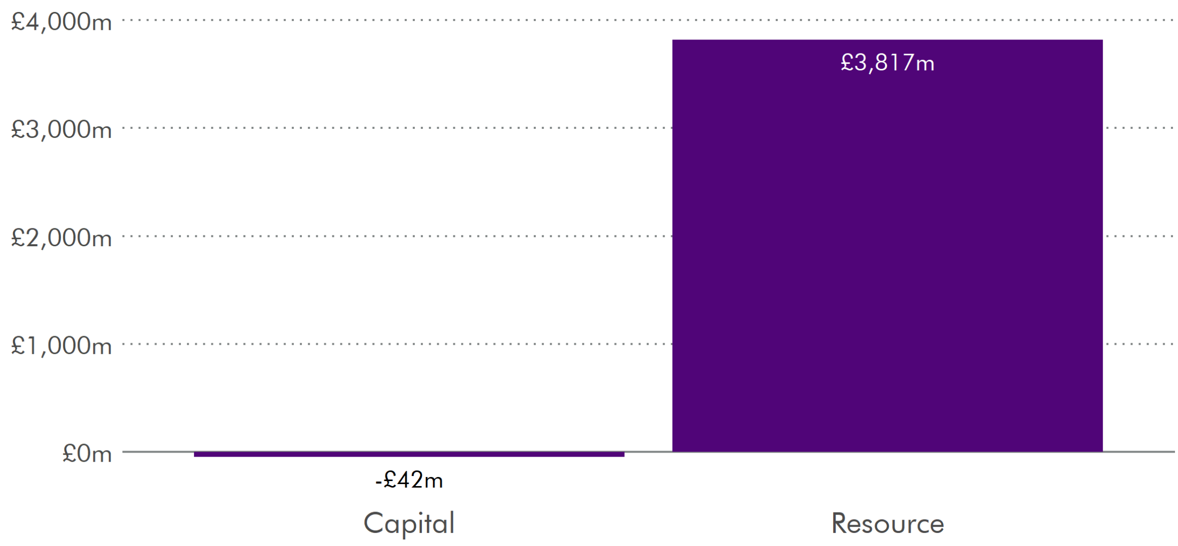
Figure 3: Allocation of TME, 2021-22



Source: Scottish Budget 2021-22

Figure 4 below shows the absolute change in Resource and Capital between 2020-21 and 2021-22.

Figure 4: Absolute Change in Resource and Capital, 2020-22 to 2021-22

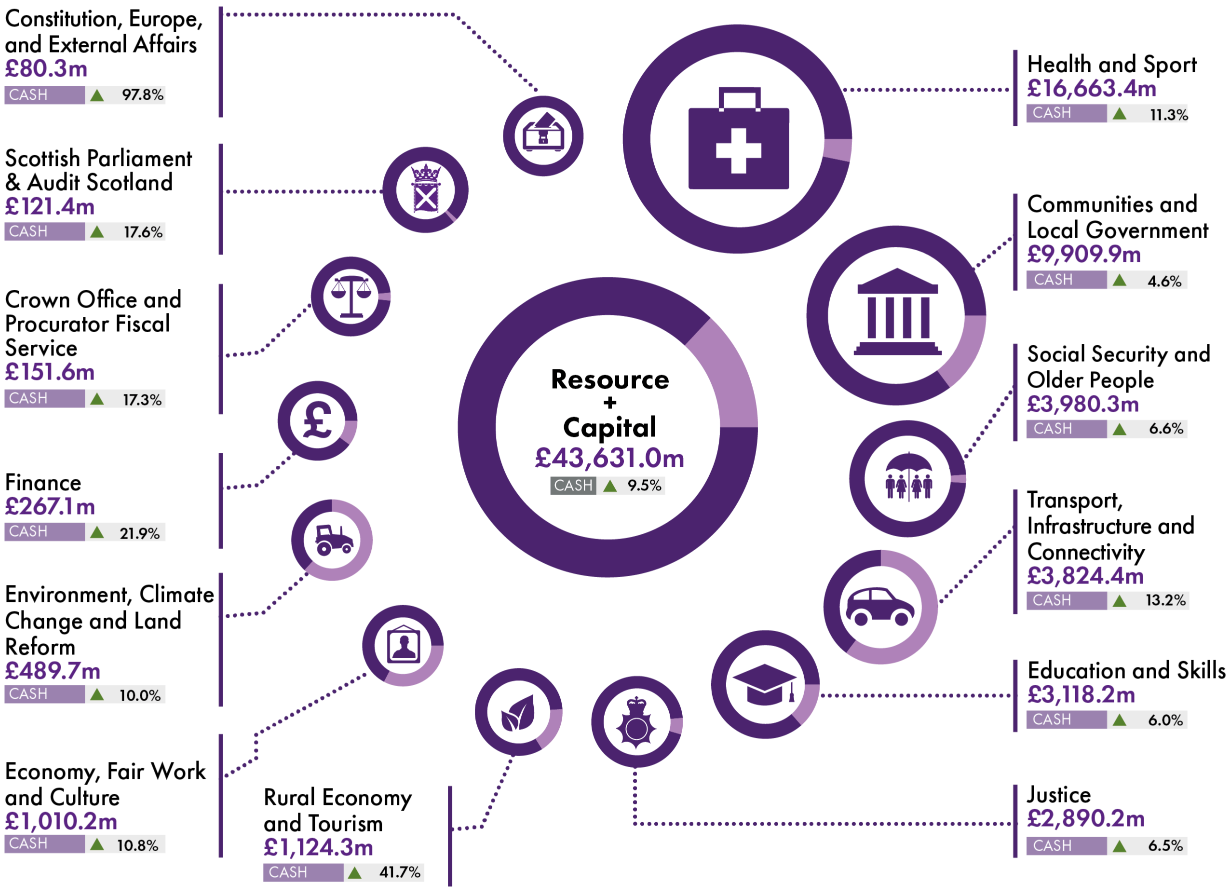


Source: Scottish Budget 2021-22

Portfolio allocations

Resource and Capital allocation to portfolios for 2021-22, and how they have changed on the previous year, are presented in figure 5.

Figure 5: Fiscal Resource and Capital, including financial transactions, combined by portfolio, 2021-22



Source: Scottish Budget 2021-22

Figure 5 shows Resource and Capital spending by portfolio and their cash terms change in 2021-22. Key points to note are as follows:

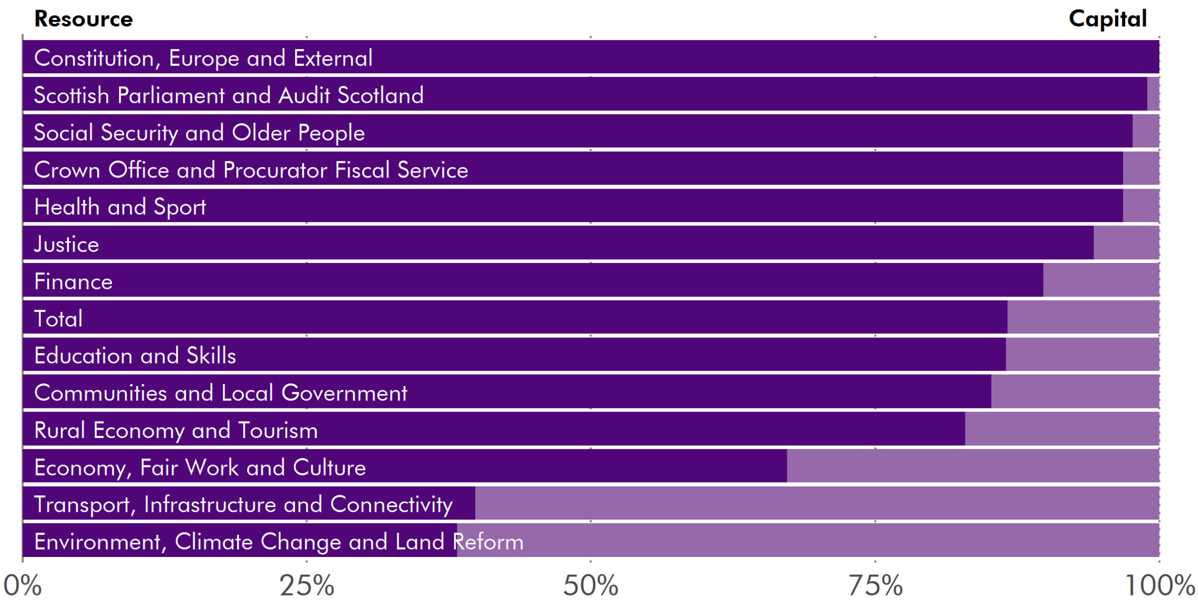
- Health and Sport is the largest portfolio, comprising 38% of the discretionary spending power (Resource and Capital) of the Scottish budget in 2020-21.
- The next largest portfolio is Communities and Local Government which comprises just under 23% of the Resource and Capital spend combined, although this does not include Non-Domestic Rates Income (NDRI), which is in AME but forms part of the local government settlement. Local government, and the settlement to local authorities, will be the subject of a forthcoming SPICe briefing.
- All portfolios will receive extra resource in 2021-22 when COVID-19 allocations are taken into account.
- The largest percentage increase (97.8%) goes to the Constitution, Europe and External Affairs portfolio, in large part due to an increase of £33.9 million for the Scottish Parliamentary elections.
- The lowest cash terms growth goes to Communities and Local Government (4.6%) (although again it should be noted this does not include NDRI), Education & Skills (6.0%) and Justice (6.0%).

Resource and Capital allocations

Figure 6 below shows the split between Resource and Capital by portfolio. This shows that most portfolios are heavily weighted towards funding day-to-day spending commitments.

The Environment, Climate Change and Land Reform and Transport, Infrastructure and Connectivity portfolios have the highest proportion of budget comprising Capital expenditure (around 60%).

Figure 6: Resource and Capital split by portfolio, 2021-22



Source: Scottish Budget 2021-22

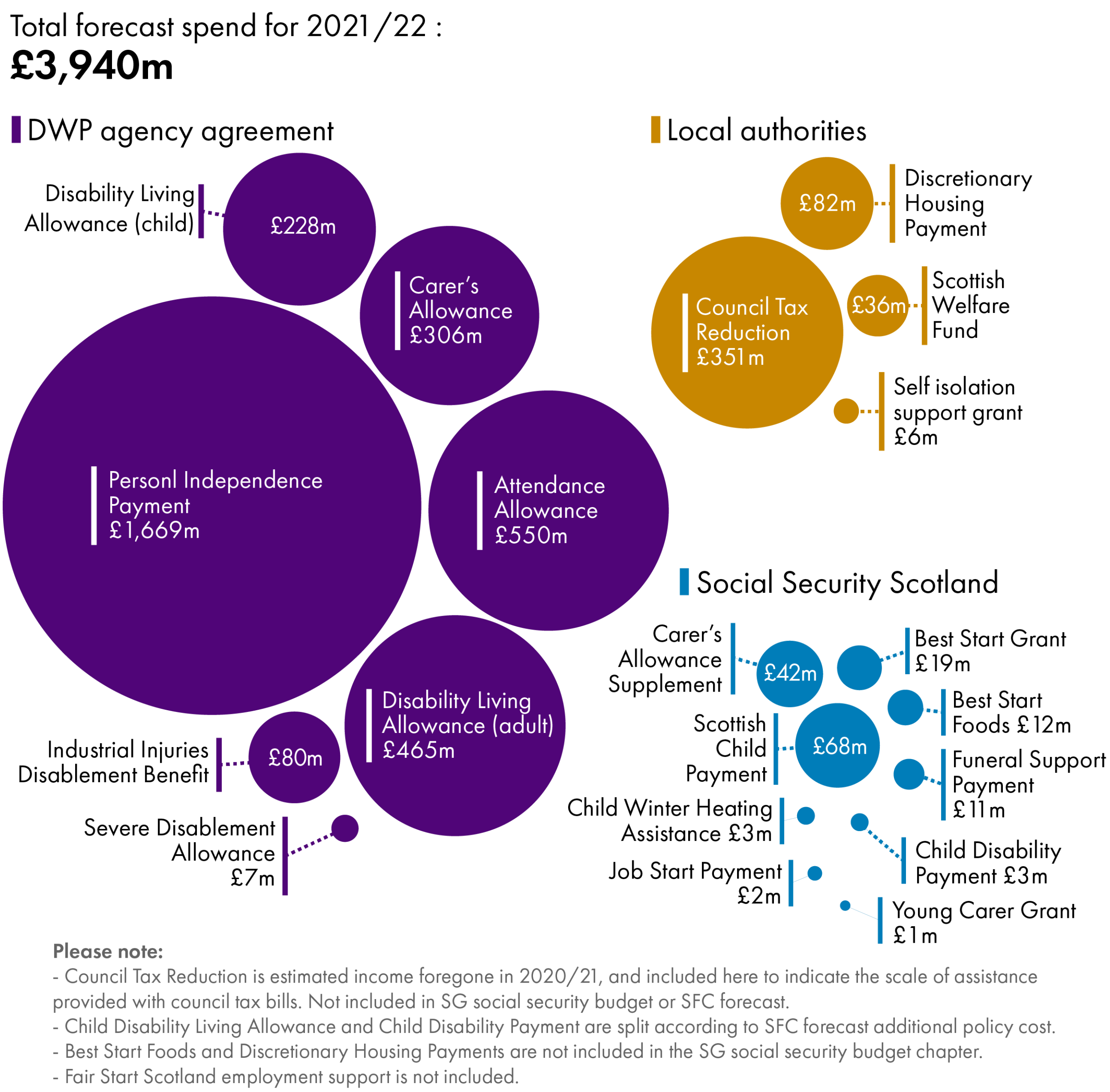
Social Security

With the devolution of certain Social Security powers by Scotland Act 2016 came over £3 billion of spending power via an upward Block Grant Adjustment (BGA) to the Scottish Budget. However, it also brought with it increased budgetary risks, as any spending over and above the BGA must be found from other resources.

In 2021-22 the BGA addition to the Scottish Budget for Social Security is £3,310 million. However, the Social Security spend in the next year is forecast by the SFC as being over £300 million higher, at £3,614 million. This is partly due to introduction of new benefits specific to Scotland, such as the Scottish Child Payment.

Figure 7 shows the various Social Security powers now devolved to the Scottish Parliament by size. The Council Tax reduction figure of £351 million is estimated income forgone, so not included in the Social Security forecast spend figure mentioned above.

Figure 7: Social Security allocations by size, 2021-22



Source: Scottish Budget 2021-22

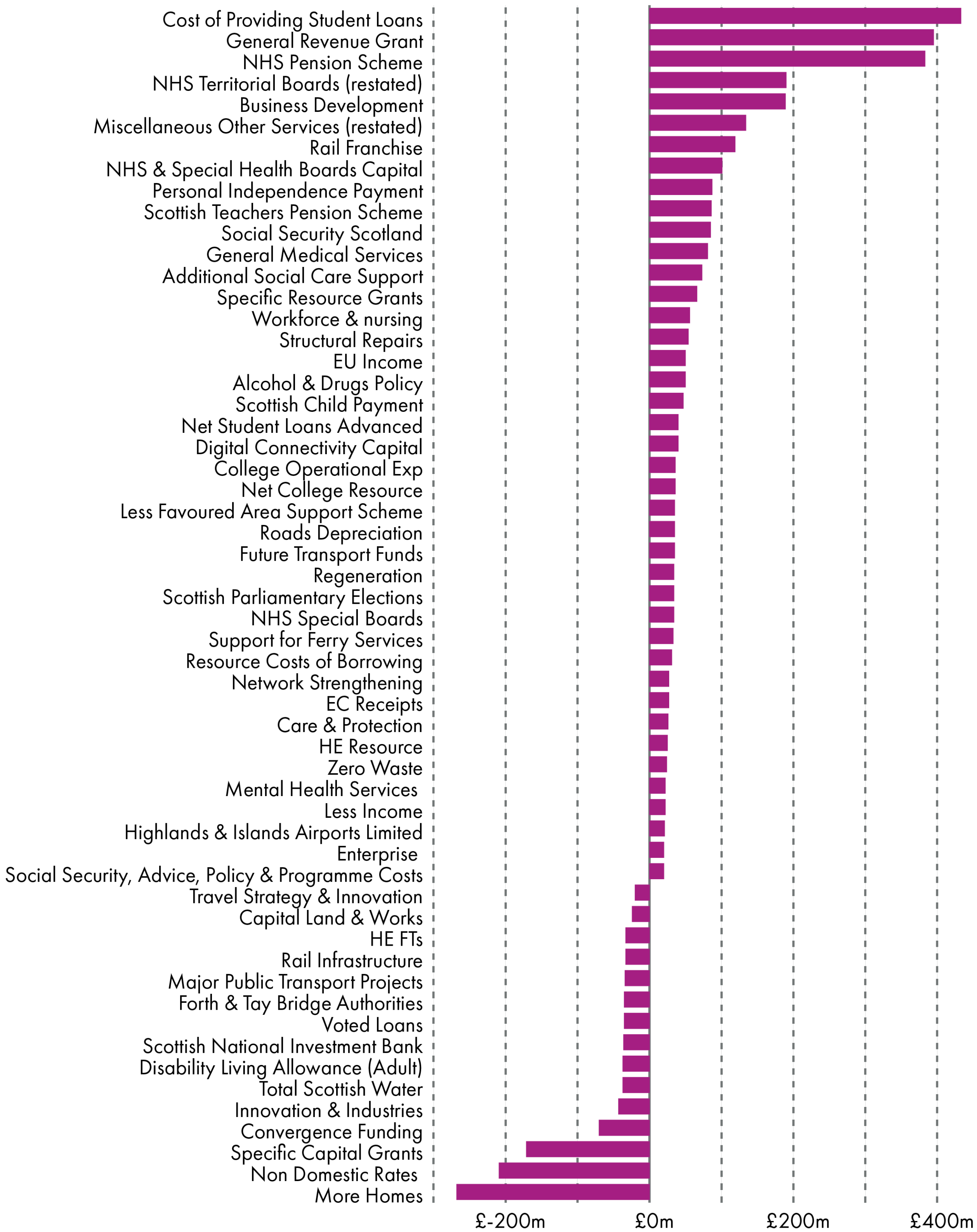
Largest Budget increases and decreases

Figure 8 presents the largest level 3 budget line increases and decreases in 2021-22 compared with the previous year.

There are large increases for Student loans and NHS pensions, which are not fully explained in the document, although both are AME items, and so fully funded by the UK Government. The local government General Revenue Grant increases by just under £400 million and the NHS Territorial Boards also receive a sizeable increase.

The cuts to Non-Domestic Rates as a response to the pandemic explains the fall in that line. The largest reduction is in the More Homes budget line, which falls by just under £270 million. The Budget document notes that the reduction in the Financial Transactions budget has had an impact on the Scottish Government's housing programme.

Figure 8: Largest cash terms changes, 2020-21 to 2021-22, £ million



*Graph excludes changes between +£20m and -£20m

Source: Scottish Budget 2021-22

Taxation policies and revenues

Income Tax

Income Tax proposals

The Scottish Government set out its proposals for Income Tax from April 2021 as part of the Scottish Budget 2021-22. These need to be approved by a Scottish Rate Resolution, which must precede Stage 3 of the Budget. Income Tax then cannot be changed during the financial year. This year, due to the delayed UK Budget, the Scottish Government has had to set it its own Income Tax policy without knowing what the UK government is proposing to do.

Very minor changes are proposed, with no changes to the rates and all thresholds other than the Top Rate threshold increasing by 0.5% (CPI inflation as at September 2020). The proposed rates and bands are shown below.

Table 4: Proposed Scottish tax bands and thresholds, 2021-22

Bands	Band name	Rate (%)
Over £12,570* - £14,667	Starter	19
Over £14,667 - £25,296	Basic	20
Over £25,296 - £43,662	Intermediate	21
Over £43,662 - £150,000**	Higher	41
Above £150,000**	Top	46

* Assumes individuals are in receipt of the standard UK personal allowance (£12,570 in 2021-22)

** Those earning more than £100,000 will see their personal allowance reduced by £1 for every £2 earned over £100,000

The SNP's manifesto for the 2016 Scottish elections included a commitment to implement an "effective personal allowance" of £12,750. The Scottish Government is not able to change the personal allowance as this is determined at UK level. However, the Scottish Government had intended to make changes that would have had the same effect as increasing the personal allowance to £12,750. This would have been achieved by introducing a zero rate tax band between the UK personal allowance and £12,750. The Fraser of Allander Institute [5] estimate that this would have cost more than £80 million. However, the budget document states that the Scottish Government has decided not to do this due to the "unprecedented circumstances".

At the UK Spending Review in November 2020, the UK government announced its intention to increase the personal allowance and UK Higher Rate threshold in line with CPI inflation (0.5% at September 2020). On this basis, comparisons with the rest of the UK (rUK) for 2021-22 assume an rUK income tax policy as set out in Table 5. It is also assumed that the tapering of the personal allowance is unchanged i.e. those earning more than £100,000 will see their personal allowance reduced by £1 for every £2 earned over £100,000. It is possible that the UK government could announce further changes to its own income tax policy at the UK Budget on 3 March 2021.

Table 5: Assumed rUK tax bands and thresholds, 2021-22

Bands	Band name	Rate (%)
Over £12,570* - £50,270	Basic	20
Over £50,270 - £150,000**	Higher	40
Above £150,000**	Additional	45

* Assumes individuals are in receipt of the standard UK personal allowance (£12,570 in 2021-22)

** Those earning more than £100,000 will see their personal allowance reduced by £1 for every £2 earned over £100,000

Income tax revenues

The Scottish Fiscal Commission (SFC) forecast that, with the proposals set out in the budget,non-savings non-dividend (NSND) income tax revenues will total £12,263 million in 2021-22. Forecasts for subsequent years, based on no change in policy other than uprating of thresholds in line with inflation, are shown in Table 6.

Table 6: NSND income tax forecasts, 2021-22 to 2025-26, £ million

	2021-22	2022-23	2023-24	2024-25	2025-26
NSND income tax	12,263	12,907	13,481	14,080	14,718

The SFC estimates for 2021-22 are lower than had been previously forecast, in large part due to the impact of the COVID-19 pandemic, which is forecast to reduce employment in 2021-22, with a resulting reduction of £458 million in forecast income tax receipts for the year. This reduces the funding available to the Scottish Government in 2021-22, although if the forecast turns out to be too pessimistic (or too optimistic), there will be reconciliations in future years.

The Scottish Government's plans to pay a £500 bonus to all NHS and social care workers [6] in the current financial year (2020-21) will have a favourable impact on income tax revenues as these payments will be treated as taxable earnings. The Scottish Government estimated that the policy would cost £180 million. According to the SFC, it will also generate an estimated £48 million in income tax revenues in 2020-21, which will act to offset the costs of the scheme.

Impact on individuals

Income tax at various levels of earnings under the Scottish Government proposals is shown in Table 7. The proposals mean that all Scottish taxpayers will pay less income tax in 2021-22 than they did in 2020-21. However, the differences are very small – only around £14 over the year for those on incomes below £25,000, rising to just over £60 per year for those earning more than £44,000. Much of this change comes from the UK Government's plans to increase the personal allowance to £12,570, rather than the Scottish

Government's own policy decisions.

When compared with rUK income tax policy, Scottish taxpayers earning less than around £27,000 are paying just under £21 less income tax than they would in the rest of the UK. This accounts for 54% of all Scottish taxpayers. However, those earning more than £50,000 will be paying at least £1,500 more income tax per year than they would in the rest of the UK.

Table 7: Differences between Scottish and rUK income tax, 2021-22

Annual earnings	Scottish Government proposals 2021-22 income tax paid - £ per year	Difference compared with 2020-21 - £ per year	Difference compared with rUK - £ per year
15,000	465	-14.12	-20.97
20,000	1,465	-14.12	-20.97
25,000	2,465	-14.12	-20.97
30,000	3,512	-15.50	26.07
35,000	4,562	-15.50	76.07
40,000	5,612	-15.50	126.07
45,000	6,930	-61.90	443.67
50,000	8,980	-61.90	1,493.67
55,000	11,030	-61.90	1,597.67
60,000	13,080	-61.90	1,647.67
65,000	15,130	-61.90	1,697.67
70,000	17,180	-61.90	1,747.67
75,000	19,230	-61.90	1,797.67
80,000	21,280	-61.90	1,847.67
85,000	23,330	-61.90	1,897.67
90,000	25,380	-61.90	1,947.67
95,000	27,430	-61.90	1,997.67
100,000	29,480	-61.90	2,047.67

National Insurance contributions

Decisions on national insurance contributions (NICs) are made by the UK Government, but will interact with the Scottish Government's decisions on NSND income tax to determine overall tax rates. NICs are linked to UK tax thresholds and the NIC rate drops from 12% to 2% at the UK higher rate threshold, which is expected to be £50,270 from April 2021. This means that Scottish taxpayers who earn between the proposed Scottish higher rate threshold (£43,662) and the rUK higher rate threshold (£50,270) will pay 41% income tax and 12% NICs on their earnings between these two amounts – a combined tax rate of 53%.

Devolved Taxes

This section sets out the impact of the Budget on devolved taxes other than Non-Savings Non-Dividend (NSND) income tax.

Land and Buildings Transaction Tax

Land and Buildings Transaction Tax (LBTT) has been devolved to the Scottish Parliament since April 2015 and replaced UK Stamp Duty Land Tax. This tax is applied to residential and non-residential land and building transactions where a chargeable interest is acquired, including commercial leases. There is also an Additional Dwelling Supplement (ADS) which applies to residential purchases of second homes.

As part of the response to the COVID-19 pandemic, the Scottish Government announced a temporary increase to £250,000 for the nil rate for residential LBTT, which was due to expire on 31 March 2021. The Scottish Government confirmed that LBTT would return to the pre-COVID rates and did not propose any further changes to LBTT tax rates in this Budget (including maintaining the first-time buyers relief, which extends the nil rated band to £175,000). Table 8 below sets out the rates for residential LBTT.

Table 8: LBBT residential band and rates

Residential Band	Thresholds	Rate
Nil rate band	Up to £145,000	0%
First rate	£145,001 to £250,000	2%
Second rate band	£250,001 to £325,000	5%
Third rate band	£325,001 to £750,000	10%
Fourth rate band	Above £750,000	12%

The ADS rate of 4% applies to all transactions above £40,000. There is a commitment to review this in the next parliament, including the time it takes to sell previous residences and issues for joint buyers.

In addition to the rates for residential purchases, LBTT is also charged on non-residential purchases and leases, as per the thresholds and rates set out in Table 9 and 10 below.

Table 9: LBTT non-residential sales bands and rates

Non-residential sale band	Thresholds	Rate
Nil rate band	Up to £150,000	0%
First rate	£150,001 to £250,000	1%
Second rate band	Above £250,000	5%

Table 10: LBTT Non-residential lease band bands and rates

Non-residential lease band	Thresholds (based on net value)	Rate
Nil rate band	£150,000	0%
First rate	£150,001 to £2,000,000	1%
Second rate band	Above £2,000,000	2%

Scottish Landfill Tax

Scottish Landfill Tax (SLT) is a devolved tax on the disposal of waste to landfill, which replaced UK Landfill Tax in Scotland from 1 April 2015 following the passage of the Scotland Act 2012 and the subsequent Landfill Tax (Scotland) Act 2014.

In the Budget the Scottish Government announced that the standard rate and the lower rate will both rise by 2.7% and 3.3% as set out in Table 11 below. Landfill site operators can continue to contribute to the Scottish Landfill Communities Fund, a tax credit scheme. The 2021-22 Budget maintains the credit rate at a maximum of 5.6% of an operator's tax liability.

In September 2019, the Cabinet Secretary for Environment, Climate Change and Land Reform announced that full enforcement of the ban on sending biodegradable municipal waste to landfill would be delayed until 2025, in response to concerns that the only way local authorities could meet the deadline would be to export waste to England. In the Climate Change Plan 2018-2032 update [7] , the Scottish Government clarified that this ban would be in effect from 31 December 2025.

Table 11: Landfill tax bands and rates

	2019-20	2020-21	2021-22	2021-22 % increase
Standard rate	£91.35	£94.15	£96.70	2.7%
Lower rate	£2.90	£3.00	£3.10	3.3%

Block Grant Adjustment

Since the devolution of tax and social security powers introduced by Scotland Act 2016, there has been a need to adjust the Scottish Government's block grant from the UK Government to reflect the fact that Scotland generates tax revenues and incurs expenditure on social security benefits.

Changes to the Scottish Government's block grant will still be determined by the Barnett formula, which reflects changes to UK spending areas that are devolved to the Scottish Parliament. The block grant is then adjusted to reflect the retention of some tax revenues in Scotland, and the transfer of new social security powers.

In relation to taxes, the initial block grant adjustment (BGA) was equal to the UK Government's tax receipts generated in Scotland in the year immediately prior to devolution. In subsequent years, the BGA for taxes has been calculated according to indexation mechanisms agreed as part of the Fiscal Framework [8] .

The differences between the BGA and the SFC's forecasts will reflect

- different tax and social security policies set by the Scottish and UK Governments
- different economic conditions
- different forecast methodologies used by the SFC and the OBR.

BGAs remove funding where the Scottish Government is now raising its own tax revenue and add funding where the Scottish Government is responsible for social security payments.

To understand how much more or less the Scottish Government has to spend, with certain taxes or benefits devolved to Scotland we can compare BGAs with SFC forecasts.

With the Scottish Budget again preceding the UK's this year, the BGAs have been made on a provisional basis and are based on the OBR's November 2020 economic assumptions. The SFC's forecasts, on the other hand, are based on more up-to-date information. When updated BGAs are published alongside the UK Government's Budget in March, the Scottish Government will have the option of applying these or the provisional BGAs, depending on which is more beneficial to the Scottish Budget. BGAs and forecasts are then reconciled at a later date with outturn information, and applied to the Budget.

The Budget document shows that the provisional BGAs for Income Tax and fully devolved taxes in 2021-22 are £12,398 million. The SFC's equivalent forecasts total £12,937 million, which is £539 million more than the BGA. This means that the Scottish Budget is £539 million better off than it would be without tax devolution. Of this £539 million figure, £475 million comes from the Income Tax forecast/BGA differential.

On these tax forecast and BGA diffferentials, the SFC state:

> “ Differences between the BGA and revenue could reflect differential performance of the respective economies and also policy differences. However, there have been no policy changes in either the UK or Scotland that would affect 2021-22 revenues, nor do we forecast a significant divergence in overall economic performance. We believe therefore that the difference between forecast tax revenues and the BGA largely arise because of the significant uncertainty around COVID-19 and its effects on the data and judgements used in our and the OBR’s income tax modelling. The timing of the two forecasts will also have had an effect: specifically the second national lockdown happened after the OBR’s November forecasts.”

As mentioned above, in 2021-22 the BGA addition to the Scottish Budget for Social Security is £3,310 million. However, the Social Security spend in the next year is forecast by the SFC as being over £300 million higher, at £3,614 million. This is partly due to introduction of new benefits specific to Scotland, such as the Scottish Child Payment. This means BGAs could be revised which will be reflected in reconciliations in future years.

Reconciliation of forecasts to actual data

We already knew before the Budget was published that 2021-22 spending would be reduced by around £300 million to reconcile the Income Tax [9] and other devolved powers’ outturn figures with original forecasts.

To manage this reduction, the Scottish Government is planning to borrow the full amount (£319 million) which will need to be repaid in subsequent years.

There was better news regarding future Income Tax reconciliations, however, with the SFC providing indicative figures for future Income Tax reconciliations. For the first time since non-savings non-dividend (NSND) Income Tax was devolved, reconciliations are forecast to be positive over the next few Budgets – totalling £74 million for 2019-20 (to be applied to the 2022-23 Budget) and £127 million for 2020-21 (to be applied to the 2023-24 Budget). As noted above, these figures could change once the OBR updates its forecasts alongside the UK Budget in March.

The Scottish Fiscal Commission forecasts

The Scottish Fiscal Commission's (SFC) main forecast publication, Scotland's Economic and Fiscal Forecasts January 2021, was published alongside the Scottish Budget for 2021-22. The SFC's forecasts are an important component in determining the total budget available to the Scottish Government to spend in each financial year. In this section, we summarise some of the key economic trends from the SFC's detailed economic forecasts .

SFC's forecasts are generally based on calendar years, unless otherwise stated. Thus, for example 2021 Q4 refers to the period October to December 2021.

Treatment of COVID-19 in forecasting

SFC's previous forecasts were published in February 2020, when it was still unclear the extent to which COVID-19 would shut down both the Scottish and global economies, at a scale never witnessed before.

In their new January 2021 forecasts, SFC has had to make a number of crucial judgements around COVID-19 that impact significantly on the economic outlook. Despite the development and roll-out of vaccines, the SFC expect both the Scottish and UK Governments to keep public health measures in place for much of 2021. They expect no quick return to "normality" for 2021-22. Notable assumptions around COVID-19 include:

- There are no further extensions to the current job protection schemes due to end at the end of April 2021.
- No subsequent waves with significantly elevated numbers of new COVID-19 cases and deaths following the 2020 Q4 to 2021 Q1 second wave.
- From 2021 Q2, they assume cases and excess deaths will gradually fall to the levels seen from June to September 2020.
- By 2021 Q4 the virus is suppressed to the extent that strict health control measures are no longer required – it is managed like a normal virus within the UK. Some continuing international travel restrictions may be required from time to time.

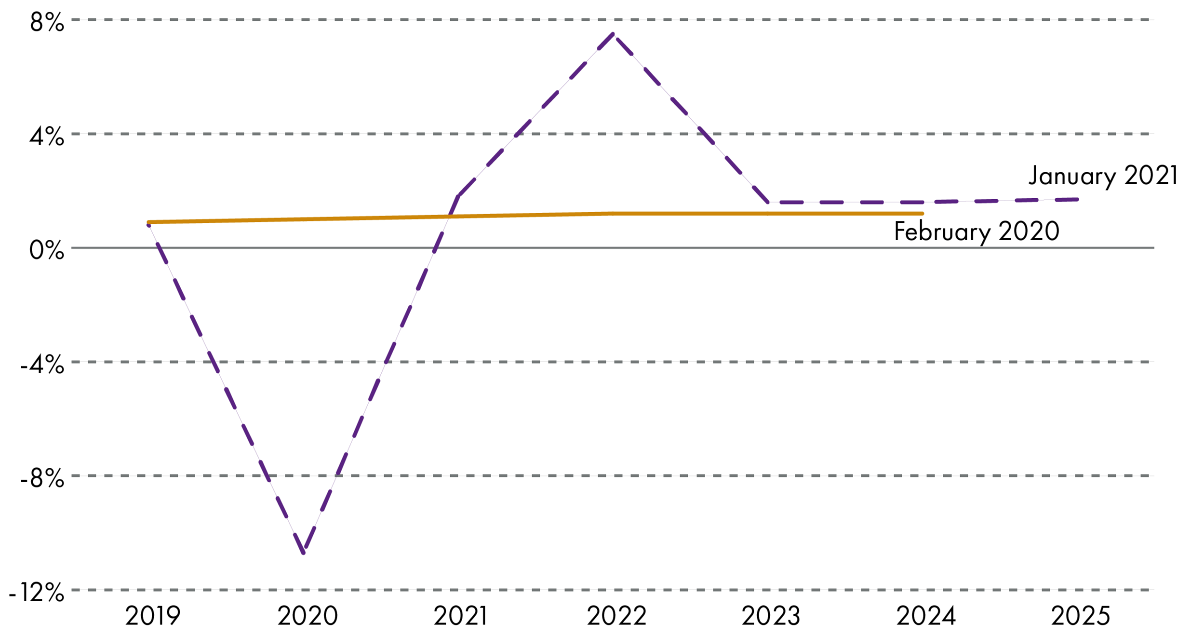
SFC acknowledge a materially different pathway of COVID-19 and restrictions relative to their assumptions would mean the pathway of the economy, taxes and social security spending could be significantly different from their forecasts.

GDP forecast

The Scottish and UK economies are both expected to contract by around 11% in 2020, as a result of the COVID-19 crisis. SFC expect GDP to fall in 2021 Q1 by around 5% but for 2021 as a whole have forecast growth of 1.8%, picking up to 7.5% in 2022. This is mainly fuelled by household consumption, as higher-income consumers who accumulated savings during the lockdown months start spending again.

Figure 9 shows current headline GDP growth forecasts (annual percentage change) in comparison to SFC's forecast from February 2020. This illustrates the unprecedented impact COVID-19 had had on the Scottish economy in comparison to the relative steady state forecast a year previous.

Figure 9: Comparison of Scottish Fiscal Commission GDP forecasts at this years and last years budget



Source: Scottish Fiscal Commission Fiscal Update – January 2021

Scottish GDP isn't expected to recover to pre-COVID-19 levels until the start of 2024. SFC estimate that Scottish GDP in 2025 will still be 4% below where they expected it to be in their February 2020 forecast.

SFC's longer term outlook for the economy looks different from their previous forecasts due to the long-lasting effects of the pandemic on the Scottish economy. The main factors driving these changes include:

- the long-run unemployment rate increases from 4.0 to 5.5% in 2020, gradually moving to 4.4% at the start of 2023
- the population aged 16 and over is 0.5% lower
- productivity is around 2% lower.

Some of these factors are discussed in more detail in the section on wider economic factors. In terms of Brexit, SFC note the deal between the UK and the EU is within the range of their previously expected outcomes, thus they continue to use the same assumptions. Assumptions used in forecasting were:

- new trading arrangements with the EU and others slow the pace of import and export growth
- the UK adopts a tighter migration regime than that currently in place.

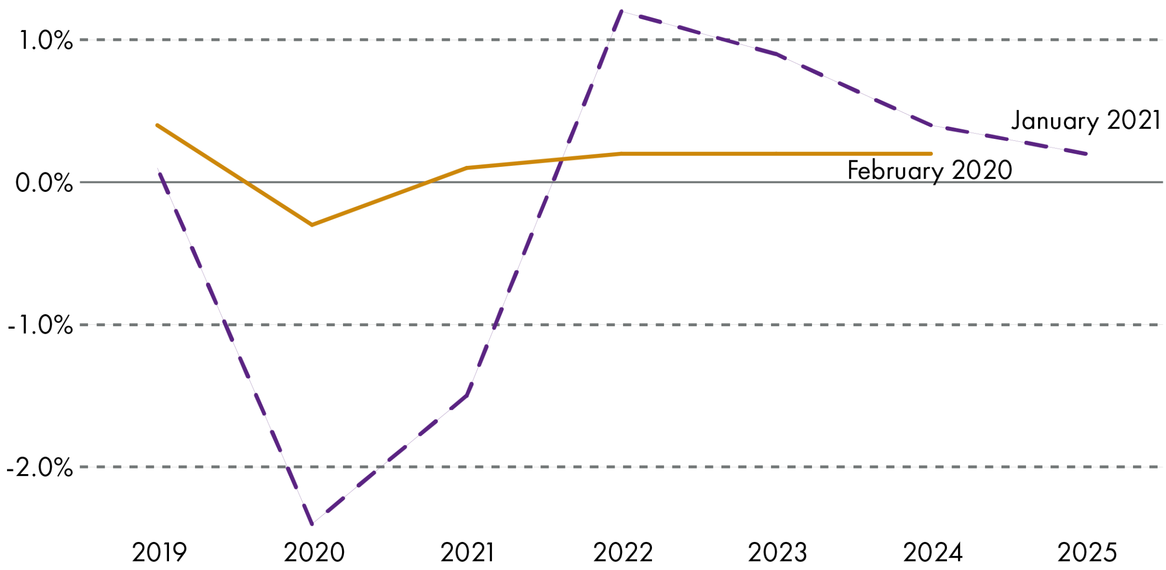
Wider economic factors

Employment

SFC note that the UK Government's Coronavirus Job Retention scheme has largely, but not completely, protected the labour market from the economic consequences of the pandemic. SFC has assumed that there are no further extensions to the current job protection schemes due to end at the end of April 2021.

And as a result, over the period 2020 Q3 to 2026 Q1 SFC expect the unemployment rate to peak at 7.6% in 2021 Q2 once the furlough schemes end. They have revised down their forecasts of employment growth in 2020 and 2021 to account for the effects of COVID-19 on the labour market. However, from then onwards, unemployment is expected to decline as the economy recovers, as illustrated in the chart below.

Figure 10: Comparison of Scottish Fiscal Commission employment forecasts at this year's and last year's Budget



Source: Scottish Fiscal Commission Fiscal Update – January 2021

Earnings

SFC forecast nominal average earnings growth of 2.5% in 2020 and 2.6% in 2021, both revised down from February 2020. Similarly, long-run forecasts of average nominal earnings growth have been revised down. This reflects assumptions on lower productivity growth, lower public sector pay growth and higher unemployment compared to previous SFC forecasts.

Table 12: Average nominal % earnings growth, forecast comparison, January 2021 and February 2020

Forecast	2019	2020	2021	2022	2023	2024	2025
February 2020	2.8	3.0	3.1	3.2	3.3	3.3	
January 2021	*4.2**	2.5	2.6	2.4	2.7	3.0	3.3

Italic cells refer to outturn available at time of publication.

Productivity

SFC's estimate of productivity (output per hour) growth in Scotland remains low and has been downgraded further relative to previous forecasts.

- Estimates of pre-COVID trend productivity growth in the period 2016 to 2019, were revised down reflecting the latest outturn data.
- Forecasts of productivity have been revised down in light of the COVID-19 crisis.

SFC has forecast zero productivity growth in 2020, to growth of 1.2% in 2024, and 1.6% in 2025. SFC state that their estimate for 2025 Q1 is around 2% lower compared to February 2020. This COVID-19 productivity scarring figure is similar to the OBR's estimate for the UK published in its November 2020 forecast.

Table 13: Trend productivity % growth, forecast comparison, January 2021 and February 2020

	2018	2019	2020	2021	2022	2023	2024	2025
February 2020	*0.2**	0.3	0.6	0.9	1.1	1.2	1.3	
January 2021		*0.0**	0.0	0.2	0.4	0.8	1.2	1.6

Italic cells refer to outturn available at time of publication.

Other economic factors

Other notable economic factors explored by SFC included population projections and economic capacity.

Unlike past SFC forecasts where ONS population projections were the basis for modelling, in this forecast SFC has developed bespoke population projections which account for COVID-19. For migration, they assume zero net international migration in the year to mid-2021, transitioning to zero per cent net EU migration from mid-2022. These new population projections result in lower trend GDP relative to the projections that were used in February 2020 by 0.5% in 2025 Q1.

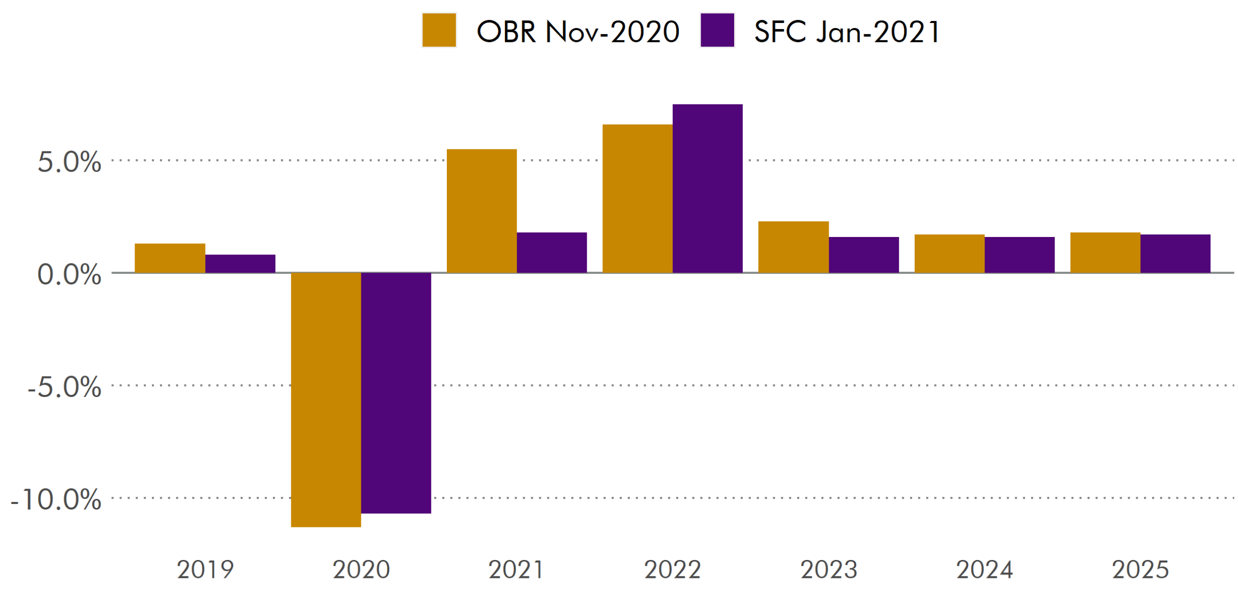
SFC believe that there will be significant spare capacity in the economy at the start of forecast period. While SFC has reduced their estimate of trend GDP, actual GDP fell by far more in 2020. This leaves capacity for actual GDP to increase rapidly until it meets their new estimate of trend GDP

UK comparison and Scotland-specific economic shock

UK comparison

The Scottish Budget has been set before the UK Budget has been published and therefore there is not a comparable set of OBR forecasts. The OBR's most recent November 2020 forecasts [10] were made before the current lockdown, and so took a more optimistic view of prospects for the economy. Comparing SFC's forecasts to the OBR's November forecasts for the UK, generally SFC is expecting slower growth in Scottish GDP, as shown in Figure 11.

Figure 11: Comparison between SFC January 2021 Scotland and OBR November 2020 UK GDP % growth rates



Source: Scottish Fiscal Commission Fiscal Update – January 2021

Scotland-specific economic shock

As mentioned previously, for the first time SFC predict that a Scotland-specific economic shock, as defined by the fiscal framework, is expected to occur. To recap, the criteria for an economic shock are:

- annual GDP growth in Scotland, on a four-quarters-on-four-quarters basis is below 1.0%
- four-quarters-on-four-quarters growth in Scotland is 1.0 percentage point or more below the UK.

The fiscal framework provides additional borrowing and Scotland Reserve powers for Scotland in the event of a Scotland-specific economic shock.

As already highlighted, the OBR's November 2020 forecasts were made before the current lockdown, and so took a more optimistic view of prospects for the UK economy in 2021 than SFC has took.

SFC believe trends for both Scottish GDP and UK GDP are broadly similar. It is thought most of the difference between SFC's forecasts for Scotland and the OBR's UK forecasts is likely to be accounted for by the fact that the two forecasts were based on different announcements about what health measures would be in place in early 2021. The Scotland-specific economic shock may not be present once the OBR updates its forecasts in March 2021, or once outturn data are available.

The additional borrowing and Scotland Reserve powers, as a result of the Scotland-specific economic shock, mean:

- The resource borrowing limit for forecast error increases from £300 million to £600 million for the next three financial years.
- The annual drawdown limits from the Scotland Reserve are removed for the same period. Even if forecasts or outturn data no longer trigger a shock in 2021-22, the relaxation of limits will not be revoked.

The use of borrowing and reserves in 2021-22 are discussed in the introductory sections of this briefing.

Linking SFC forecasts to the budget

The SFC's fiscal forecasts directly determine the Scottish Government's Budget, particularly around tax and social security.

In total the SFC are forecasting £15.6 billion of the Scottish Budget will be raised by devolved tax in 2021-22 (£15 billion in 2020-21).

SFC forecast in 2021-22 the Scottish Government will spend £3.6 billion on devolved social security (£3.4 billion in 2020-21).

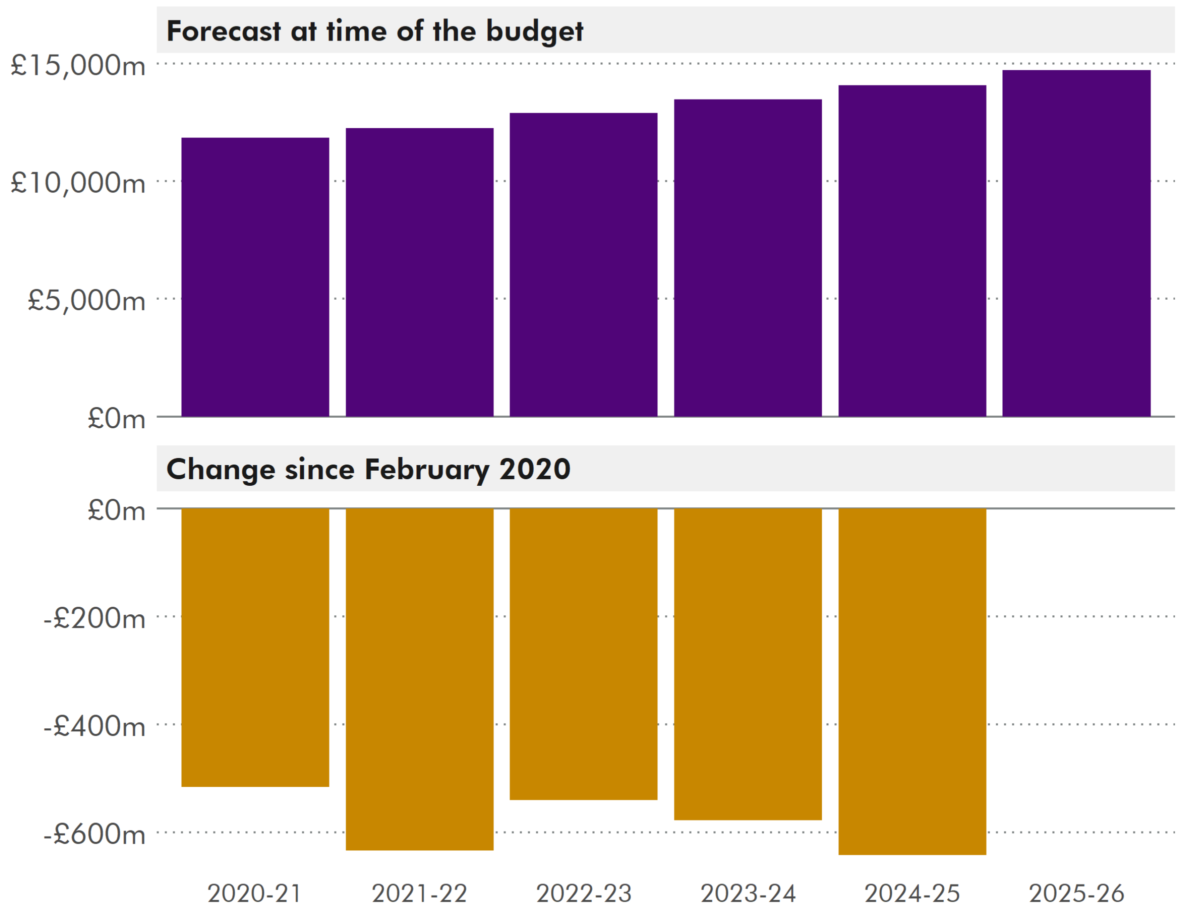
SFC forecasts for devolved taxes

This section gives an overview of the latest forecasts from the Scottish Fiscal Commission for revenues from devolved taxes and how these have changed since the last publication (February 2020, to accompany the last Scottish Budget). In an earlier section of the briefing we look in more detail at the Scottish Government's tax policies.

The significant changes in the economic context since the last forecasts were produced in February 2020 means that expected revenues from all devolved taxes are materially lower than at the time of the last Budget, in almost all years. In total, revenues from devolved taxes are expected to be £1.6 billion lower in 2020-21 compared to the forecast from February 2020, with decreases in expected revenues from Non-Domestic Rates (NDR) and Income tax responsible for £1.4 billion of this change.

Forecast Non Savings Non Dividend (NSND) Income Tax

Figure 12: Non Savings Non Dividend (NSND) Income Tax forecast and change from previous budget's forecast



Source: Scottish Fiscal Commission Fiscal Update – January 2021

Revenues from NSND Income Tax are forecast to rise by 3.5% in 2021-22, 5.2% in 2022-23 and then around 4.4% over the remainder of the forecast period. This compares to growth of 2.4% between 2018-19 to 2019-20 – however outturn data is only currently available up to 2018-19. Compared to the February 2020 forecast, revenues from NSND Income Tax are expected to be significantly lower over the forecast years. Revenues are expected to be £516 million lower in 2020-21 than forecast in February, and then a total of £2.4 billion lower over the next four financial years.

Table 14: Changes in SFC NSND Income Tax forecast since February 2020

£m	2020-21	2021-22	2022-23	2023-24	2024-25
Change since February 2020	-516	-634	-540	-578	-642

The main driver of these differences is the updated economic context since the last forecast. The SFC have also made some changes to their methodology; they have aligned their forecast to better reflect HMRC's Real Time Information (RTI) data. Outturn for 2019-20 is matched to this data, while the forecast years extrapolate the growth rate based on the available data. Previous forecasts were based on the most recent outturn

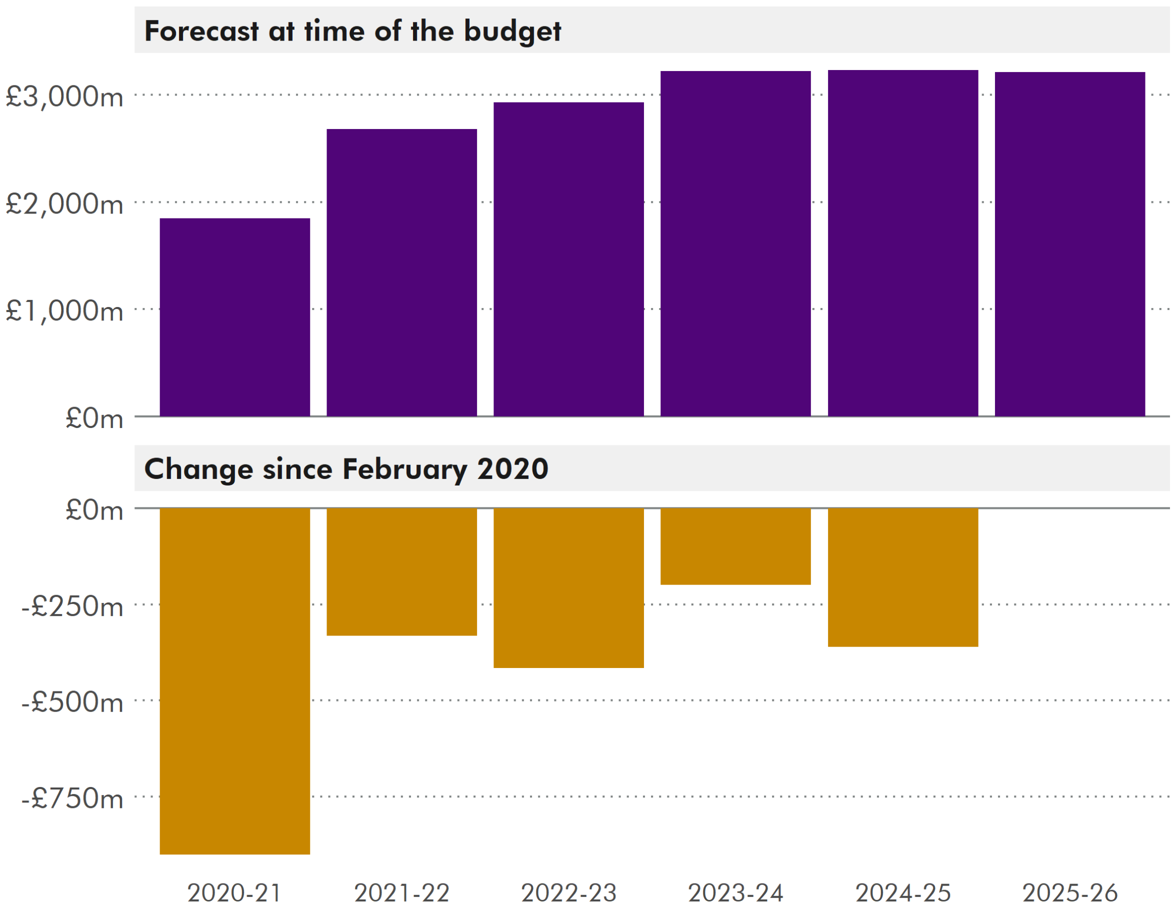
Pay as you Earn (PAYE) data, but uncertainty due to COVID-19 and the improved consistency between RTI and PAYE data has allowed the SFC to use RTI. This is a more timely source of data, which allows the SFC to better model the impact of more recent events such as the furlough scheme. The impact of this modelling change is to reduce forecast revenues from NSND Income Tax by £340 million in 2021-22.

While the forecast for revenues from NSND Income Tax has reduced, COVID-19 has also impacted expected revenues from UK Income Tax. The change in the block grant adjustment (BGA) for 2021-22 related to income tax is +£954 million. The net effect of the difference in the SFC and the BGA forecasts is an additional £320 million for 2021-22, which if it does not change in subsequent forecasts will boost Scottish Government spending power in 2023-24. It is worth noting that the BGA is based on the November 2020 forecast from the OBR, which is more optimistic, as it preceded the winter lockdown and the discovery of the more transmissible variant of COVID-19. It is therefore likely that the BGA forecast will change at the time of the UK Budget in March.

The SFC explain that there is no single reason why such a material difference exists between their forecast and the OBR's. They note that this is a period of exceptional uncertainty which presents challenges in measuring the true scale of the economic impact from COVID-19, while significant interventions such as the furlough regime have to some extent broken the link between labour market data and the wider economy.

Non-Domestic Rates

Figure 13: Non-Domestic Rates forecast and change from previous budget's forecast



Source: Scottish Fiscal Commission Fiscal Update – January 2021

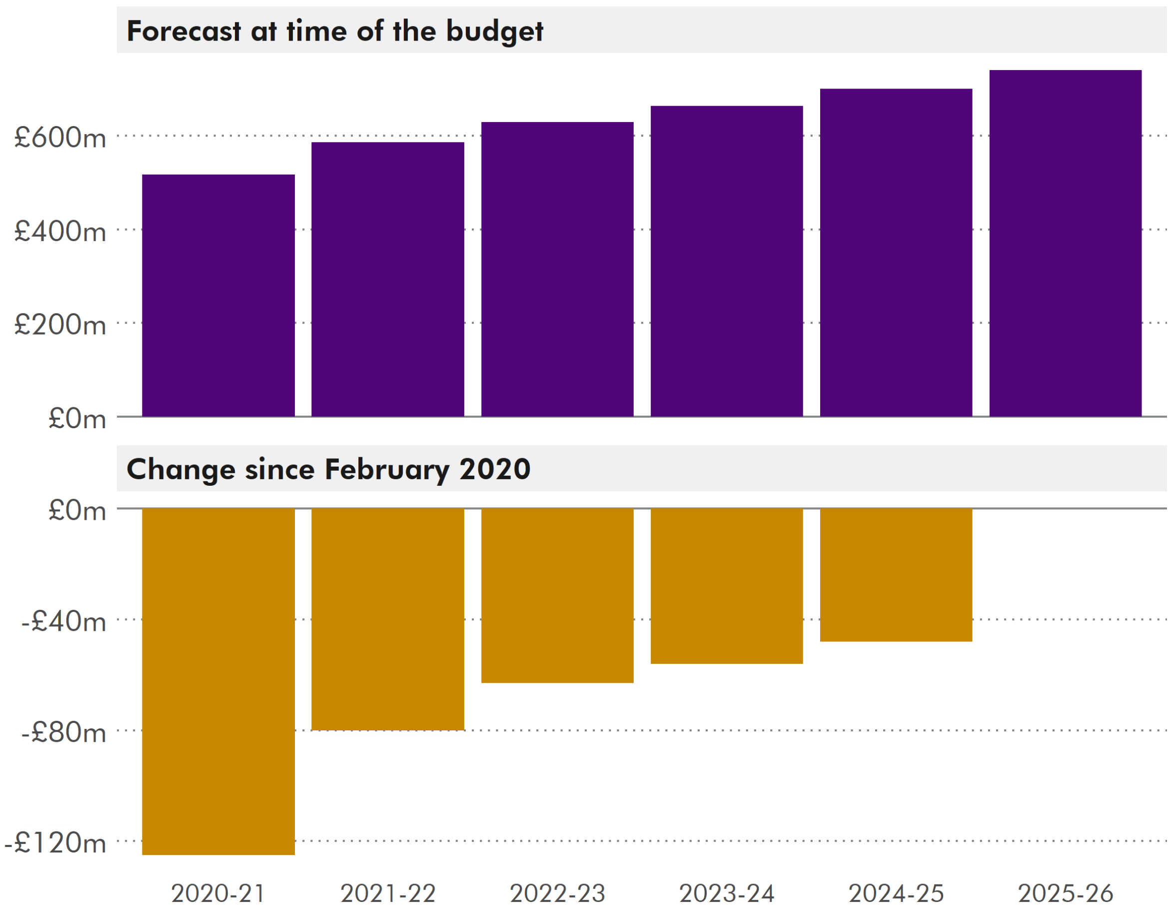
Forecast revenue from NDR in 2020-21 is £901m lower than at the time of the February 2020 forecast, and remains lower than expected throughout the forecast period (a total of £1.3bn lower from 2021-22 to 2024-25). Of this reduction, £331 million relates to the announcement of setting the poundage at 49.0p, and a further £185m relates to the 100 per cent relief announced for retail, hospitality and aviation for three months until June 2021. The remainder of the difference is driven by some small updates to the tax forecasting approach by the SFC, but mainly by the change in the broader economic forecasts over the period.

Table 15: Changes in SFC NDR forecast since February 2020

£m	2020-21	2021-22	2022-23	2023-24	2024-25
Change since February 2020	-901	-332	-415	-199	-360

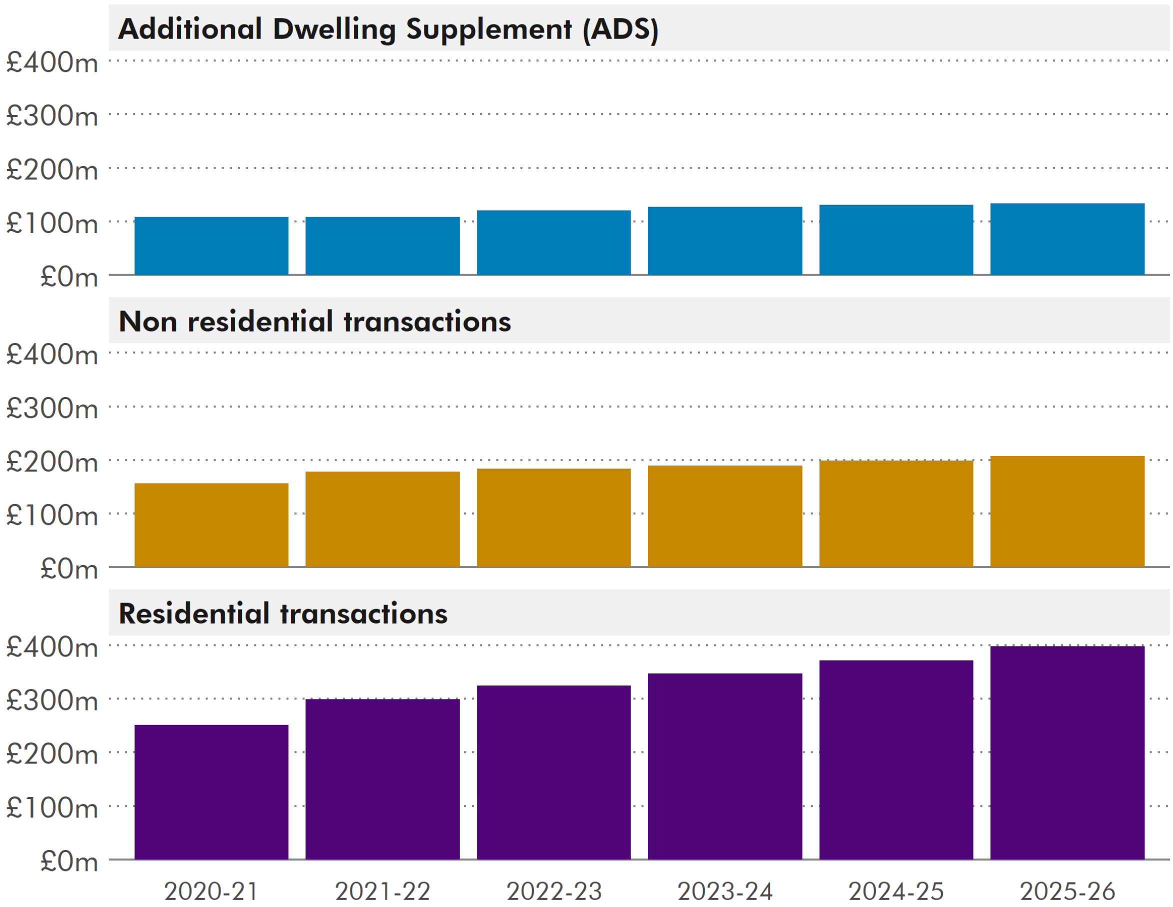
Land and Buildings Transaction Tax

Figure 14: Land and Buildings Transaction Tax forecast and change from previous budgets forecast



Source: Scottish Fiscal Commission Fiscal Update – January 2021

Figure 15: Land and Buildings Transaction Tax forecast by dwelling type



Source: Scottish Fiscal Commission Fiscal Update – January 2021

LBTT forecast is reduced each year, largely due to the changes in the economic forecast since February 2020. The expected revenues from LBTT in 2020-21 are £125 million lower, while between 2021-22 and 2024-25 revenues are £247 million lower. The revised economic forecast is slightly offset by an update to the medium-term projection for residential house price growth in Scotland, from 2% to 3%.

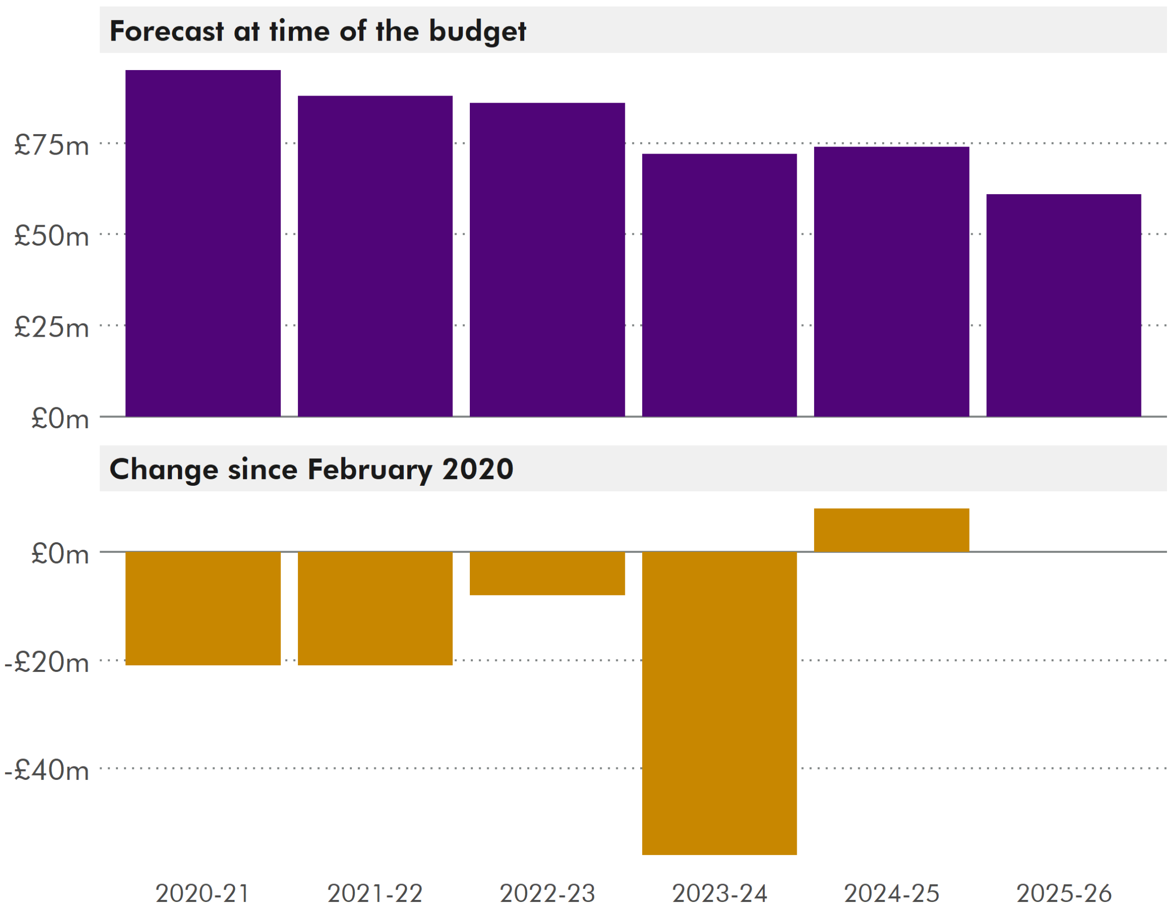
However, in 2020-21 the block grant adjustment (BGA) is forecast to be £166 million lower than in February 2020, which implies a net impact of positive £44 million on the Budget. This positive BGA is due to the difference in the temporary uplift to the nil rate band in Scotland compared to England and Wales; the Scottish Government set the nil rate band at £250,000, while elsewhere in the UK it rose to £500,000. This meant that revenues from Stamp Duty fell more in the UK than revenues from LBTT did in Scotland. This reconciliation will not take place until outturn data is available, and so will not impact the Scottish Budget until 2023-24.

Table 16: Changes in SFC LBTT forecast since February 2020

£m	2020-21	2021-22	2022-23	2023-24	2024-25
Change since February 2020	-125	-80	-63	-56	-48

Scottish Landfill Tax

Figure 16: Scottish Landfill Tax forecast and change from previous budget's forecast



Source: Scottish Fiscal Commission Fiscal Update – January 2021

Revenues from SLT are £21 million lower than February 2020 forecast in 2020-21, and £36 million lower in total between 2021-22 and 2024-25. Delay to full enforcement of the biodegradable municipal waste landfill ban until 31 December 2025 (which was previously assumed to be 1 January 2025) means that forecast revenues are £8 million higher in the final year. The changes in the earlier years' forecasts are largely driven by the updated economic forecasts, coupled with some relatively minor updates to the tax model.

Table 17: Changes in SFC SLT forecast since February 2020

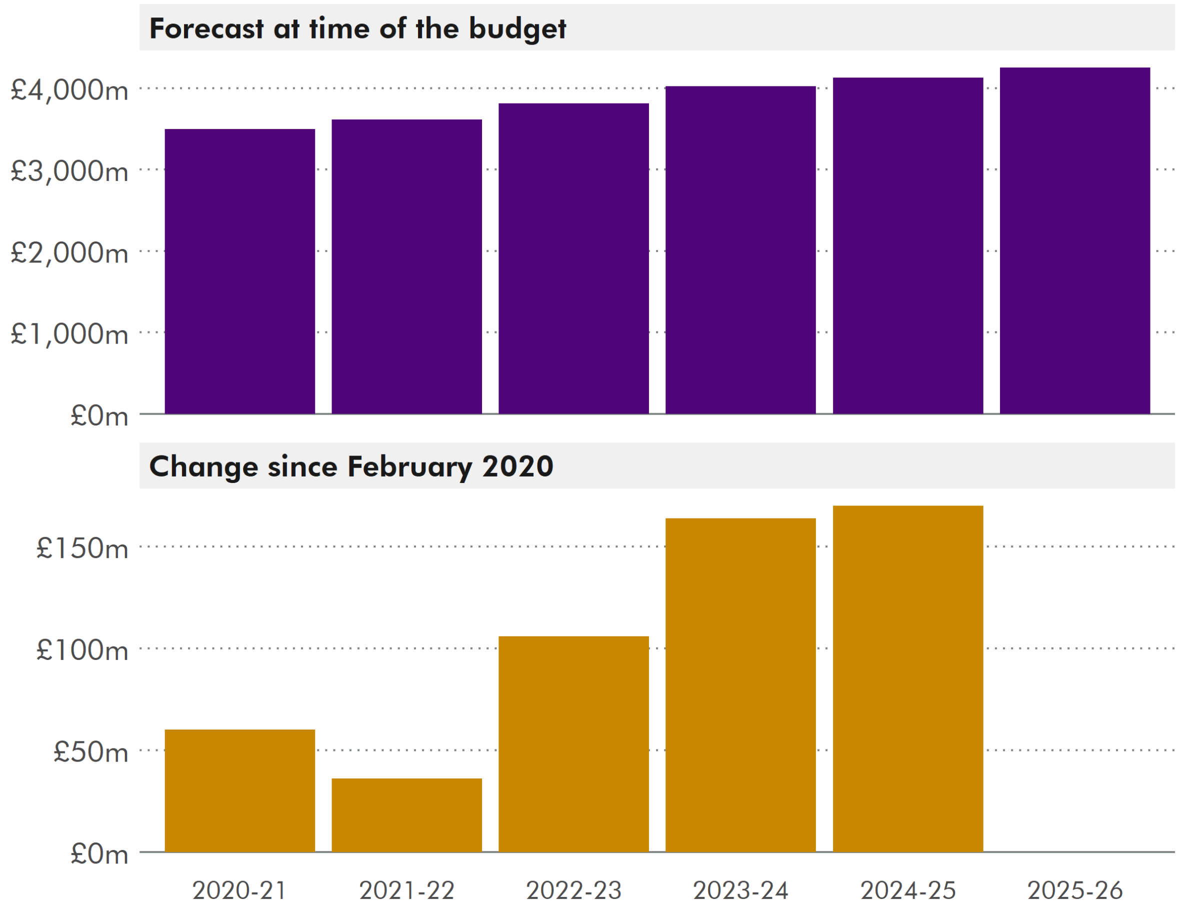
£m	2020-21	2021-22	2022-23	2023-24	2024-25
Change since February 2020	-21	-21	-8	-7	8

Social Security forecasts

The increase in social security spending over the forecast period is driven by more people receiving support each year, and the uprating of payments to keep pace with inflation. This forecast does include the impact of new social security payments which have already been launched, such as the Scottish Child Payment which starts on 15 February 2021.

However, it does not include the impact of planned Scottish replacement payments which have not yet launched, such as the Adult Disability payment. Once the details of these programmes are finalised, the SFC will forecast their costs. The change in the forecast since February 2020 is mostly because of the Scottish Government’s response to COVID-19, particularly in the earlier years of the forecast.

Figure 17: Social Security forecast and change from previous budgets forecast



Source: Scottish Fiscal Commission Fiscal Update – January 2021

Capital and Infrastructure

The 2021-22 capital budget from HM Treasury is £4,973 million, a 5% increase in cash terms compared with 2020-21. The Scottish Government plans to further boost capital expenditure in 2021-22 through a combination of mechanisms:

- Using maximum borrowing powers (£450 million).
- Using Financial Transactions (FT) funding from the UK Government and recycling receipts received from previous loans made using FTs (£552 million).
- Capital grant receipts and other income (£63 million).
- Making use of innovative finance mechanisms, such as the Growth Accelerator and Tax Incremental Financing (£50 million).

These additional financing sources will mean total capital investment in 2021-22 of £6,089 million, which is 2.5% lower than the equivalent planned infrastructure spending for 2020-21 (£6,243 million). This reduction is primarily driven by lower Financial Transactions funding. Further detail on the sources of funding for infrastructure spending is given below.

The Scottish Government's National Infrastructure Mission [11] set out plans to increase annual infrastructure investment so that annual investment is £1.56 billion higher in 2025-26, when compared with a 2019-20 baseline. The plans set out in the 2021-22 Budget represent a £791 million increase on 2019-20.

In recent years, the Scottish Government has used revenue financing to increase the level of infrastructure investment that can be achieved through the capital budget alone. Revenue financing means that the Scottish Government does not pay the upfront construction costs, but is committed to making annual repayments to the contractor, typically over the course of 25-30 years. The Scottish Government previously used a model known as the Non-Profit Distributing (NPD) model but has proposed introducing a modified version of the NPD model, known as the 'Mutual Investment Model' (MIM). This shares a number of features with NPD but is adjusted so that it meets the requirements for such investment to be treated as private sector investment and therefore paid for out of revenue budgets over a longer timeframe. However, the budget document does not make any reference to the use of MIM.

The Scottish Government published a draft Infrastructure Investment Plan [12] in September 2020. A final version is due to be published in the first week of February 2020, along with a project pipeline and a Capital Spending Review.

Borrowing powers

The Scottish Government is able to borrow up to £450m in each year for capital investment, up to a cumulative total of £3 billion. The Budget sets out plans to borrow the maximum £450 million in capital borrowing to support infrastructure expenditure in 2021-22.

Borrowing powers were also used in full in 2017-18 and 2019-20, but only £250 million was borrowed in 2018-19. In 2020-21, the Scottish Government had intended to borrow the full £450 million but has since revised these plans to a lower borrowing total of £300 million. According to the SFC, the borrowing plans for 2021-22 bring the cumulative total borrowing to £2.2 billion.

The SFC is required to assess the reasonableness of the Scottish Government's borrowing plans. They assessed the Scottish Government's capital borrowing plans as reasonable but noted that, if borrowing continues at the maximum of £450 million per year, then the £3 billion cap will be reached by 2024-25, which will limit future options. The Scottish Government's Medium-Term Financial Strategy [13] sets out the Scottish Government's intention to ensure that a minimum of £300 million capital borrowing headroom is available to be drawn down in the year following the period covered by the National Infrastructure Mission (2026-27). This sets a further limitation on borrowing options in the next five years.

Financial Transactions

The 2020-21 Budget includes £552 million for financial transactions (FTs), including repayments. Net financial transactions (after adjusting for receipts) total £408 million. These FTs relates to Barnett consequentials resulting from a range of UK government equity/loan finance schemes (primarily the UK housing scheme, Help to Buy) and have been a regular source of funding since 2012-13. The Scottish Government has to use these funds to support equity/loan schemes beyond the public sector, but has some discretion in the exact parameters of those schemes and the areas in which they will be offered. This means that the Scottish Government is not obliged to restrict these schemes to housing-related measures and is able to provide a different mix of equity/loan finance.

The amount allocated by HM Treasury to the Scottish Government in FT funding has reduced by around two-thirds in 2021-22, from £606 million in 2020-21 to £208 million in 2021-22. However, the Scottish Government plans to draw down £200 million from the reserve built up from previous underspends on FT allocations and will also supplement the FT budget by using repayments from earlier FT loans.

For 2021-22, a total of £142 million (gross) in financial transactions has been allocated to housing-related schemes. The Scottish Government is also providing equity/loan finance support in areas other than housing. In 2021-22, £204 million (gross) in FTs will also be used to provide upfront capitalisation for the Scottish National Investment Bank.

Individual tables in the budget document show the following profile for financial transactions. Negative figures indicate portfolio areas where repayments are planned to exceed new investment.

Table 18: Financial transactions (net), £ million

Portfolio	£ million
Communities and Local Government	100.0
Economy, Fair Work and Culture	200.0
Education & Skills	22.1
Transport, Infrastructure and Connectivity	54.6
Rural Economy and Tourism	28.6
Finance	3.3
Environment, Climate Change and Land Reform	(0.6)
Total	**408.0**

The Scottish Government will be required to make repayments to HM Treasury in respect of these financial transactions. These repayments will be spread over 30 years, reflecting the fact that the majority of FT allocations relate to long term lending to support house purchases and the construction sector. The repayment schedule is based on the anticipated profile of Scottish Government receipts. A repayment to HM Treasury of £25 million in respect of FTs is scheduled for 2021-22.

Innovative financing

The Growth Accelerator (GA) and Tax Incremental Financing (TIF) are local authority led financing schemes, whereby projects are financed through borrowing in the expectation that future uplifts in local taxation income will fund the repayments. The Scottish Government has identified plans to finance £50 million of investment through such mechanisms but no further details are given.

Revenue financing and the 5% cap

Annual repayments resulting from revenue financed projects and borrowing come from the Scottish Government's resource budget. The Scottish Government has previously committed to spending no more than 5% of its total resource budget (excluding social security) on repayments resulting from revenue financing (which includes NPD/hub, previous PPP contracts, regulatory asset base (RAB) rail investment) and any repayments resulting from borrowing. Previous budget documents have shown performance against this commitment, but no information is provided in the document this year. The lack of any plans to use revenue financing for infrastructure investment in 2021-22 will mean less pressure on this cap, although increased borrowing will mean higher future repayments linked to this.

Local government

This section of the briefing sets out a high-level summary and analysis of the local government budget for 2021-22. The Local Government Finance Circular, which details the specific allocations to local authorities, is due for publication on Monday 1 February 2021. A dedicated SPICe briefing setting out the settlement for local authorities in more detail will follow.

The total allocation to local government in the 2021-22 Budget is £11,108.2 million. This is mostly made up of General Revenue Grant (GRG) and Non-Domestic Rates Income (NDRI), with smaller amounts for General Capital Grant and Specific (or ring-fenced) Resource and Capital grants.

Once Revenue funding within other portfolios (but still within the totals in the Finance Circular, and detailed in Budget 2021-22 table 5:14) is included, the total is £11,620.4 million. Further, once a number of funding streams attached to particular portfolio policy initiatives, but outside the totals in the Circular are included, the total rises to £12,251.8 million.

Within these global headline figures, the breakdown between different interpretations for revenue and capital, and the year to year change, has been subject of much parliamentary debate in recent years. The following sections set out these figures.

The Scottish Government guarantees the combined GRG and distributable NDRI figure, approved by Parliament, to each local authority. If NDRI is lower than forecast, this is compensated for by an increase in GRG and vice versa.

This combined Budget document figure for GRG+NDRI only (i.e. the amount of money to deliver services over which local authorities have control) increases by 1.9% in cash terms, or £185.8 million.

Once specific, ring fenced resource grants are included, then the combined figure for the resource budget increases by 2.5% in cash terms, or by £252.2 million. With the additional £259 million announced for the allocation of COVID-19 consequentials added to this, the additional funding increases to £511.2 million.

To get the £594.6 million figure quoted in the Cabinet Secretary's statement to the Parliament, the figure for "Total revenue within other Portfolios" is added to this combined sum.

Alongside the revenue budget, used to pay for public services, local government also receives a capital budget, again made up of general (i.e. discretionary) and specific (i.e. ring-fenced) grants. Overall, the total capital budget sees a decrease in cash terms this year, of -20.7% or by £161 million. This is mostly driven by a decrease in non-recurrent specific capital grants, with support for capital remaining relatively static with an increase of 2.2%, following a significant decrease between 2019-20 and 2020-21 .

In its response, COSLA drew attention to ongoing pressures faced by local authorities and highlighted that additional funding was "predominantly for Government priorities":

> “ We welcome elements of today’s announcement but overall this budget falls short of what we would consider a fair settlement for Local Government.”

In COSLA's Budget Reality 2021-22 document, released alongside its statement on the Budget, COSLA argues that, in comparison to the asks in its pre-Budget document:

> “ The settlement represents a shortfall of £362 million in core revenue funding, £20 million in core capital funding, and £511 million in non-recurring COVID-19 funding.”

Will these spending or tax proposals change?

As has happened in previous years of minority government, the Scottish Government will now attempt to strike a Budget “deal” with another political party, or parties, in the Parliament.

In previous years, deals have been struck around additional allocations to local government, or tweaks to income tax bands to generate additional resource for public spending.

Responding to the statement by the Cabinet Secretary, political parties set out areas where they are seeking change [14] . Murdo Fraser for the Conservatives called for more support for business via an extension of grant support and Business rate relief. Jackie Baillie for Labour raised the issue of funding for the Scottish National Investment Bank, as well as Local Government support and pay. Willie Rennie of the Liberal Democrats stated a wish for increased support for Mental Health Services and Patrick Harvie called for greater focus on energy efficiency and green investment programmes.

The Budget's publication marked the beginning of the Parliamentary scrutiny process. Alongside Committee scrutiny in the coming weeks, it will likely be in the bilateral negotiations between the governing and opposition parties that the changes to these Budget proposals will arise.

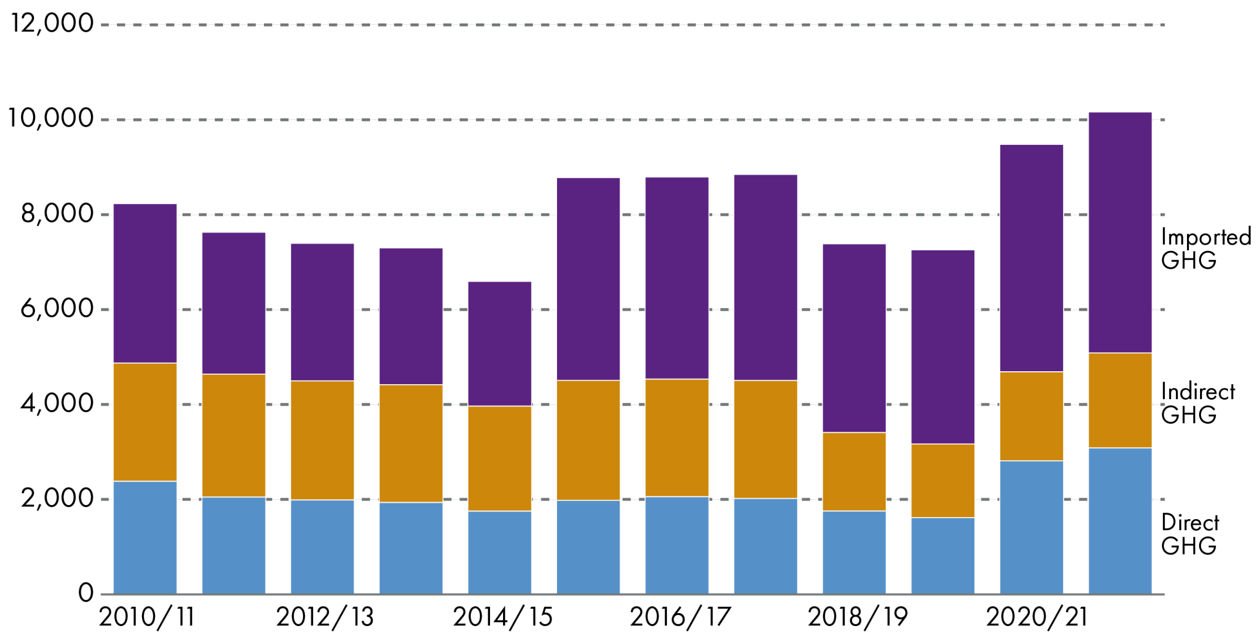
Carbon Assessment, capital taxonomy and the green recovery

Carbon Assessment of the Scottish Budget

The Climate Change Act 2009 requires the Scottish Government to provide assessments of the impacts on greenhouse gas emissions of activities funded by its budget.The Climate Change (Emissions Reduction Targets) Act 2019 also requires a carbon assessment of the Infrastructure Investment Plan.

Since 2009, twelve high-level carbon assessments of the budget have been published using an Environmentally-extended Input-Output (EIO) model to estimate emissions. This model is normally used to understand the flow of money though the economy. However, the environmentally-extended version averages greenhouse gas effects for 98 industry sectors and converts the financial inputs from the budget into expected greenhouse gas outputs. This model shows the direct, indirect and imported emissions associated with the Scottish Budget.

Figure 18: Emissions associated with the Scottish Budget since 2010-11



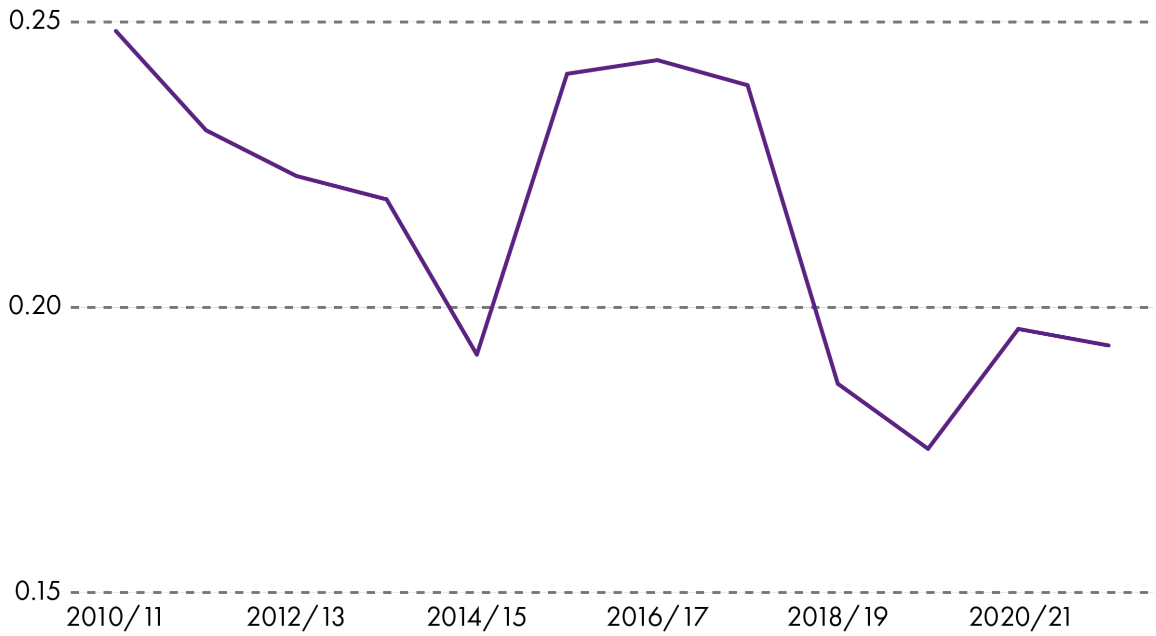
Source: Scottish Budget 2021-22

It is estimated that total emissions resulting from the goods and services purchased by the 2021-22 Budget will be 10.2 Mt (million tonnes) CO2-equivalent, a 13% increase on 2020-21 (which was estimated to have emissions of 9.0 Mt CO2-equivalent). At the time of publication, the carbon assessment for the 2020-21 Budget estimated that total emissions would be 9.5 Mt CO2-equivalent. This has been revised down to 9.0 Mt CO2-equivalent largely as a result of the updated GDP deflators, discussed earlier in this briefing**.** The updated deflator implied a lower level of activity than was originally forecast for 2020-21 due to the COVID-19 pandemic, which translates into lower levels of emissions. Conversely, the 2021-22 assessment includes the impact of some of this reduced activity returning to more normal levels.

The Scottish Government explains that the increase in emissions is almost entirely down to the corresponding cash growth in total Budget spend over the year, i.e. more spending equals more emissions. To put this into some kind of context, 10.2 $MtCO_2e$ is equivalent to 24.5% of the estimated total greenhouse gas emissions for Scotland in 2018.

The carbon intensity of the overall budget – that is the ratio of GHG emissions to £ spend, broadly supports the Government's explanation. Figure 19 below sets out the carbon intensity of the overall Scottish Budget since 2010/11. This chart uses the carbon assessment as published with the draft budget, so does not reflect changes in spending plans as a result of the Parliamentary process or changes to the carbon assessment since its publication. The calculation uses TME excluding non-cash items, and has not been adjusted to remove inflation.

Figure 19: Carbon intensity (emissions per pound spend) of Scottish Budget since 2010-11



Source: Scottish Budget 2021-22

One limitation of this model is that it does not predict the long-term outcome of spending decisions. For example, the emissions associated with the construction of a new railway line are measured. But the effect of the eventual opening of the new line on people's travel choices is not. So, these assessments help us to understand only the immediate emissions associated with Government spending decisions, and don't really help to measure whether Scotland is on track to reach "net-zero" greenhouse gas emissions by 2045. The Scottish Government acknowledge this limitation, and note in the Carbon Assessment that:

> " During Stage 2 of the Climate Change (Emissions Reduction Targets) (Scotland) Bill 2019, the Government committed to working with the Parliament to review the current processes and outputs around budget information as it relates to climate change. That review is now in progress. The aim of the review is, where feasible and proportionate within the anticipated timescales, to improve budget information on climate change – to understand and reduce spend that will 'lock in' future greenhouse gas emissions and increase alignment between the budget and climate change plans."

Taxonomy of capital spend

Since 2018-19 the Scottish Government have set out a taxonomy of the capital spend in the budget, which sets out the proportion of the spend classified as low, neutral or high carbon. In previous years this has been provided by letter to the Finance and Constitution Committee, but this year has been included in the summary of the Carbon Assessment in Annex H of the Budget document.

This analysis categorises capital expenditure as either high, broadly neutral or low carbon using a simple methodology.

Table 19: Taxonomy assessment of capital budgets

	2018-19	2019-20	2020-21	2021-22
Low	29.1%	31.8%	34.9%	36.9%
Neutral	59.3%	58.1%	56.9%	54.6%
High	11.6%	10.6%	8.2%	8.5%

The high carbon spending, which has increased slightly since last year, is entirely as a result of Transport and Infrastructure investments totalling £441.8 million. The most significant contributors to these are 'Capital Land and Works' (£155.8 million, down from £179.8 million last year), 'Network Strengthening' (£104.4 million, up from £77.5 million last year) and 'Structural Repairs' (£100 million, up from £45.7 million last year). The increases all relate to spending on motorways and trunk roads. The Scottish Government note that this increase in investment is to address a backlog, and is a direct consequence of accepting the Infrastructure Commission for Scotland's recommendation [15] that greater investment in ongoing maintenance is required. The increase in the low carbon figure is as a result of projects funded by £165 million from the £2 billion Low Carbon Fund.

As noted above, this is a relatively simple methodology which has some drawbacks. While it can be used to track whether the Scottish Government are meeting their commitment to increase the percentage of the capital budget allocated to low carbon projects in each year of the Parliament, this classification does not quantify how effective the low carbon investments are at mitigating climate change, nor does it quantify how carbon intensive any of the investments are. While we can see that the proportion of spend classified as 'high' has reduced over the last four fiscal years, the taxonomy does not tell us whether this resulted in lower emissions in each year, and crucially does not account for emissions in future years as a result of these investment decisions. Therefore, while the assessment is useful to understand the prioritisation within the Capital Budget, it does not tell us whether the Scottish Government is on track to meet their net zero targets.

The Scottish Government are aware of the limitations of this approach, and set out a planned approach in the draft Infrastructure Investment Plan published in September 2020. ClimatexChange were commissioned to explore possible replacement methodologies for assessing the consequences of infrastructure investment, and published their report in September [16] . In the Budget document, the Scottish Government notes that:

> " The Scottish Government will take this forward in conjunction with the Joint Review of Budget. Developing this new approach will form part of the five year implementation plan for our decision-making framework set out in the forthcoming Infrastructure Investment Plan. This will also support the next Climate Change Plan."

Green recovery and carbon capture investment

Although a prominent theme throughout the Budget, there were few *new* announcements made in the document relating to the 'green recovery'. Many spending commitments had already been announced in the Programme for Government (PfG), the draft Climate Change Plan update or the accompanying Climate Emergency Skills Action Plan. For example, the £100m Green Jobs Fund was previously announced in the 2020-21 PfG, with the Budget document merely confirming that the first £14m tranche will be delivered in 2021-22. Likewise, the £2 billion low carbon investment highlighted in the Budget had already been discussed in considerable detail in the PfG some months earlier.

SPICe has already discussed [17] how the shift in ambition evident in the draft Climate Change Plan update published before Christmas is very much driven by the Scottish Government's expectations regarding the development and adoption of hydrogen technology and Carbon Capture and Storage (CCS). However, what has become clear over a number of committee sessions in recent weeks is that infrastructure to transport and store CO2 should be developed quickly over the next few years.

In their submission to the Economy, Energy and Fair Work Committee, research group Scottish Carbon Capture and Storage states that "CCS infrastructure – or more accurately, infrastructure to transport and store CO_2 – does not exist yet in Scotland", and:

> " …at minimum Scotland will need on- and offshore CO_2 pipelines, between the central belt and the North East and out to the offshore storage sites, as well as potential upgrades to port and harbour facilities to enable the transport of CO_2 by ship for storage in Scottish sites."

Other than the £180 million Emerging Energy Technologies Fund announced already before Christmas in the draft CCP update, the Budget is relatively quiet about how the Scottish Government will invest in CCS infrastructure over the next few years. Perhaps there will be more detail in the Infrastructure Investment Plan, which the Cabinet Secretary reminds us "will outline a pipeline of projects that drive Scotland's resilience driving inclusive, net-zero and sustainable growth", and will be published in early February.

EU replacement funding

European Structural Funds are awarded for a seven-year period, with the final period that Scotland and the UK are involved in being the 2014-2020 budget. The UK has announced that EU Structural Funds (the European Social Fund and the European Regional Development Fund) will be replaced by the UK Shared Prosperity Fund (UKSPF), which is expected to launch during 2021. In the November 2020 Spending Review, the UK Government has pledged that the level of funding available through the UKSPF will “at least match the current EU receipts, on average reaching £1.5 billion per year”.

Under the EU schemes, the Scottish Government was the ‘managing authority’, which meant they had a key role in directing the funding in Scotland. In November 2020, the Scottish Government published plans for its management of the UKSPF in Scotland. However, these plans have been cast into doubt following the passage of the UK Internal Market Bill. In the Budget the Scottish Government note that:

> “ Across many of our communities – but particularly in rural and island areas – there have also been significant economic benefits felt through European Structural Funds. …. Following the UK’s departure from the EU, the Scottish Government has been clear that we expect to receive our full share from the replacement funding programme, the UK Shared Prosperity Fund (UKSPF) – at least £1.3 billion for a replacement seven‑year programme – with Scotland having full say over how these funds are used. Recently, however, the UK Government have announced that they will bypass the Scottish Government, delivering the UKSPF directly.”

Budget and Outcomes

As part of the 2007 Spending Review, the Scottish Government introduced a new outcomes-based National Performance Framework (NPF) to underpin the delivery of its agenda.

Following the Community Empowerment (Scotland) Act 2015, the Scottish Government is required to review its National Outcomes every five years. During the first review in 2018, the Government also took the opportunity to change the structure of the NPF and implement a series of other changes. More information about the refreshed NPF and how it could be used in budget scrutiny can be found in this 2019 SPICe Briefing.

The revised NPF has a detailed website [18] which includes information on how the NPF works, the outcomes, measuring progress and the UN Sustainable Development Goals.

The National Outcomes and the NPF feature throughout the Budget. As well as an overall introduction, each portfolio is linked to primary and secondary national oucomes. This appears to be a further development in the information provided in the previous year's Budget, and alongside the outcome information in the Equality and Fairer Scotland statement, should prove useful for committees in their budget scrutiny.

COVID-19 is the overarching theme of this year's budget. However, a quick look at the indicator performance pages shows that most of the indicators are subject to lengthy data lags. While a few indicators have 2020 data, most only go up to 2018 or 2019. In addition, although launched in 2018, 13 of the 81 indicators are still marked as either "performance to be confirmed" or "indicator in development."

In December 2020, the Scottish Government, together with COSLA, published Scotland's Wellbeing: The Impact of COVID-19 [19], which: "aims to report openly and transparently on how COVID-19 has affected progress towards Scotland's National Outcomes."

A SPICe blog published in January summarises this report and provides some possible areas for committees to explore. [20]

The Medium Term Financial Strategy

Alongside the Budget, the Government also published Scotland's Fiscal Outlook: The Scottish Government's Medium-Term Financial Strategy (MTFS). The MTFS was originally scheduled to be published in May 2020 but was delayed due to the COVID-19 pandemic. The document states that:

> " The MTFS sets out the key financial challenges and opportunities that lie ahead. It provides the context for the Scottish Budget and also sets out the new and specific context that will govern the life of the next Scottish Parliament. This context will frame the decisions of the incoming Government's strategic approach to economic and fiscal policy."

This is the third version of the MTFS. It is worth reflecting back that introduction of the MTFS follows a recommendation of the Budget Process Review Group [21] (BPRG) that the Scottish Government takes a more medium to longer-term approach to financial planning. The document was also envisaged by the BPRG as giving a focal point for parliamentary scrutiny of some of the medium term opportunities and challenges for the Scottish public finances.

As with the Budget, the MTFS is of course dominated by the pandemic and the policy response. It contains a lot of detail on the economic and fiscal outlook, drawing on the SFC forecasts and other relevant documents. It also provides some high level scenarios for the funds available for the Scottish Budget through to 2025-26. While it does not give indicative portfolio breakdowns for future years, it does provide more detail on the Government's broad priorities of:

- new, good and green jobs
- promoting lifelong health and wellbeing
- promoting equality and helping our young people fulfil their potential
- a just transition to a green economy.

While not at the level of detail that subject committees might require for detailed scrutiny, the MTFS does give rise to possible questions around the balance of spending over the medium term. And, most crucially, if the above four areas are the stated priorities of the government, and resources are constrained, which areas might well be reduced in the medium term to pay for these priorities?

Equality and Fairer Scotland Budget Statement

This is the twelfth year the Scottish Government has published an equality statement to accompany its budget [22] . The statement provides analysis of how protected characteristics (as set out in the Equality Act 2010) are affected by the 2021-22 Budget. In preparing the statement, the Government has been assisted by the Equality Budget Advisory Group, a non-statutory advisory group which has helped shape the Scottish Government's approach to budgeting since the early days of devolution.

As with much of the Budget this year, there is significant focus on the impact of COVID-19 on people and communities across Scotland. The impact of Brexit on equalities is also considered in some detail. Therefore, this year's statement looks somewhat different to previous statements, particularly with the main part of the report being devoted to an exploration of what the authors call "the ten key existing or emerging risks resulting from the COVID-19 pandemic". These key risks are:

1. Heightened risk that existing structural inequalities in the labour market will be entrenched and worsened.
2. Elevated risk of poorer labour market outcomes and disproportionate impacts on young people due to COVID-19.
3. Risk that women's unfair responsibility for unpaid care and domestic work might get worse and reduce their ability to find paid work and income.
4. COVID-19 mortality and health inequalities.
5. Drug and alcohol deaths remain unacceptably high with the impact of COVID-19 unclear.
6. High and rising mental health problems made worse by COVID-19.
7. As work, public service and home schooling moved online it highlighted a real digital divide.
8. Risk that economic impacts and decisions about Universal Credit could increase poverty and particularly child poverty.
9. Risk that gaps in attainment and skills levels will have been made worse by periods of blended and virtual learning.
10. Evidence of rising levels of domestic abuse and reporting of sexual abuse crimes against women and children as well as risk of rising hate crime due to COVID and EU Exit.

The majority of the statement looks at evidence of each risk, including the identification of any evidence gaps, and then goes on to document the policy and budget responses to each risk. Importantly for Parliamentary scrutiny, the statement also includes details of how the Government intends to evaluate policies and budget, and how it plans to close the evidence gaps.

For example, under Risk 5 – relating to drug and alcohol deaths – there is substantial evidence showing that deaths from drugs misuse have increased massively since 2013. The statement explains that the Budget includes new funding of £50 million per year for the next five years, together with new commitments around treatment and access to residential rehabilitation. However, it would perhaps have been more useful to explain how this money will be allocated and specifically how it will be used to tackle existing inequalities.

The separate Annex A (portfolio assessment of equality and fairer impacts of the Scottish Budget) was published to provide detailed analysis for each budget portfolio. This should be very useful for Parliamentary committees as they scrutinise spending plans within their remits. Interestingly, the new template includes a column exploring how reductions in spending may impact on inequalities. The nature of this year's budget means that there are very few reductions; however, it will be important to continue this focus in all future budgets when the Government may face cuts to its block grant.

Public Sector Pay

Public sector pay accounts for around half of the Scottish resource budget and so decisions on public sector pay have a major influence on overall spending. The Scottish Government published its Public Sector Pay Policy for 2021-22 [23] alongside the Budget. This primarily covers Scottish Government's own staff plus those of a number of public bodies. The Scottish Government opted not to follow the UK government's policy of a public sector pay freeze for 2021-22, instead allowing for modest pay increases. It should be noted that the UK government's policy explicitly excluded NHS staff and included a modest uplift for those earning less than £24,000.

The main features of the Scottish Government's 2021-22 pay policy are:

- a basic pay increase of 1 per cent for public sector workers who earn below £80,000
- limiting to £800 the maximum basic pay increase for those earning £80,000 or more
- continuing the requirement for employers to pay staff the real Living Wage, now set at £9.50 per hour
- a guaranteed cash increase of £750 for all staff who earn £25,000 or less.

The pay policy does not apply directly to all public sector staff. It only affects the pay of Scottish Government staff, and the staff of agencies, non-departmental public bodies (NDPBs) and public corporations, which together account for around 10% of the devolved Scottish public sector workforce (around 42,000 full-time equivalent staff). Large parts of the public sector, such as local government and the NHS are not directly covered by the Scottish Government's pay policy and pay is determined separately for these groups, although often in line with the Scottish Government's pay policy and - in some cases - with some Ministerial control.

The pay policy notes that:

> " This policy also acts as a benchmark for all major public sector workforce groups across Scotland including NHS Scotland, fire-fighters and police officers, teachers and further education workers. For local government employees, pay and other employment matters are delegated to local authorities."

The Scottish Government's Medium-Term Financial Strategywhich was published alongside the 2021-22 Budget set out some analysis of the implications of decisions on pay policy. This showed the public sector paybill totalling £15 billion in 2021-22, with the application of a 1% basic award. Each additional percentage point on the basic award adds roughly £0.15 billion to the paybill.

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