



Regional Economic Development
Local Economy Briefing 10

Next Generation First – The UK Budget March 2016

The Chancellor of the Exchequer has delivered another complicated budget. There was lots of tinkering with the tax and spending systems in ways that distracted attention from the gloomier economic numbers and the further austerity to come.

Starting with the macroeconomics (see table below), a slowing global economy, fragile financial markets and low productivity growth everywhere saw the Office of Budget Responsibility (OBR) cutting its growth and inflation forecasts and, crucially, its assessment of future productivity potential.

With employment still set to be the main engine of growth, UK real GDP is forecast to rise only 2% in 2016, (down from 2.4% as forecast as recently as early December). Yet, the OBR could still be too optimistic for this year, especially if BREXIT uncertainty increases and cuts investment and consumption more than currently expected. Sadly, only 2.1% growth is now seen as the underlying trend for this Parliament, even with a (surprising) smaller drag from trade. Moreover, inflation only returns to target (2% per annum) in 2018 – and the OBR and the Bank of England have a poor track record on this in recent years. Monetary policy, with the threat of negative interest rates hinting at prolonged resource misallocation, is not helping a return to economic sustainability.

OBR Forecasts March 2016

%ch pa	2016	2017	2018	2019	2020
Real GDP	+2.0	+2.2	+2.1	+2.1	+2.1
Employment	+1.3	+0.3	+0.6	+0.3	+0.3
Productivity	+0.7	+1.9	+1.5	+1.8	+1.8
Inflation	+0.7	+1.6	+2.0	+2.1	+2.0
Net trade	-0.4	-0.1	-0.1	-0.1	-0.1

The weaker economic forecasts affect the government finances, increasing borrowing in the near term and worsening debt ratios over the forecast period (a debt/GDP of 82.6% in 2016/17 only moves down to 74.7% in 2020/21). The fiscal surplus target is not achieved until 2019/20 – just in time



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for the next election? Against this background, government spending is set to fall from 40% to 36.9% of the economy by 2020, as government departments seek to find another £3.5bn of cost cuts per year by 2019/20.

The Treasury is aiming to get more funds (£12bn) from further measures to cut tax avoidance and evasion. Promise of a further cut in corporation tax to 17% and reductions to business rate thresholds, commercial stamp duties, and oil and gas taxes is to be offset by attacking loopholes that have been mainly exploited by large corporations. The Chancellor was selling a theme of large companies will pay more and small companies will pay less.

Other 'goodies' are offered in further moves towards devolution, for the national administrations and the English regions. From halving Severn Bridge tolls in 2018 to a combined authority for East Anglia, the Treasury offers a plethora of new devolution measures. It is not yet clear whether there is real substance in this, especially for Dorset, especially as the Chancellor confirmed his preference for helping areas with an elected Mayor.

The aim of 100% of local authority resources being raised and spent locally by 2020 is a transformation that may turn out to be highly stimulating to local engagement and reform but it can also be highly divisive. For example, it is interesting that the Treasury is cutting business rates just before they are going to be devolved to the local authorities, (starting with the GLC in a year's time).

This Budget claims growth is driven by infrastructure, education and enterprise.

- On infrastructure, the government will commission various road and rail schemes in the Northern Powerhouse (M62 widening/HS3 rail Manchester-Leeds/Manchester-Sheffield tunnel), London (cross-rail 2 but nothing on a 3rd runway) and the South West (rail resilience). Meanwhile the insurance premium tax goes up another 0.5% specifically to pay for flood defences. It is not clear how that will be funnelled locally.
- On education, all schools are to be, at least, on the way to Academy status, independent of local authorities, by 2020. Across the south,



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overnight, the reception to this proposal has been decidedly mixed. There are additional plans to boost performance in northern schools and to devise a new funding formula for all schools. On childhood obesity, the government is introducing a levy system on soft drinks in 2018 in order to promote more sport and other activities 'out of' normal school hours.

- On enterprise, class 2 national insurance contributions will be abolished in 2018, (helping the 3mn or so self-employed), most indirect taxes remain frozen, and capital gains taxes are cut from next month (base 18% to 10% and higher 28% to 20%).

Finally, with regard to personal taxes and savings, most people are helped a bit. For example, the personal income tax allowance will rise from £11,000 to £11,500 in April 2017 and the higher rate threshold will reach £45,000. The Chancellor also announced measures to help those under 40 to save, recognising the bewildering position that exists at present with pensions and other investment opportunities in a world of near-zero interest rates. A new "Lifetime ISA" will be created for the under 40s (until you are 50). As long as it is to be used for long-term savings (pensions or first-time house buying), savers can put £4,000 into this ISA per annum and the government will add another £1,000. The help to buy ISAs (which have only just started) can be rolled into this new Lifetime ISA. Also, the existing personal ISA limit increases from just over £15,000 to £20,000 in April 2017.

The 2016 budget was headlined as one that puts the "next generation first". Many parts of the Budget will come into effect later rather than sooner, however. There is a lot of detail to be worked out and many consultations to conduct before those details are finalised. Overall, the real development worry is still in the macro economy and the micro lack of productivity in particular. The negative risks now emphasised in the Budget speech could blow all the new fiscal measures and investment intentions out of the water.

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