Hunt's Spring Budget and the UK's Economic Prospects

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If last week's Spring Budget was, as some Conservative MPs had hoped, intended to herald the beginning of the campaign for the next general election, potentially on May 2nd, its impact does not will appear to have shifted the party's standing in the opinion polls.

According to polling organisation Savanta who carried out a survey following chancellor Jeremy Hunt's spring budget, the Conservatives are on 25% and Labour, on 43%, enjoy a lead of 18 points – the largest since Liz Truss's resignation – meaning it "failed to deliver a much-needed boost" (Gibbons, 2024).

Larry Elliott believes that, given the current economic circumstances, what chancellor Jeremy Hunt delivered last week was a "holding operation" in the hope of improved prospects during the summer prior to another budget when he'll deliver more measures to convince wavering voters to support his party in the general election (2024).

Nonetheless, Conservative Party MPs and members had hoped Hunt would deliver on a statement made by Rishi Sunak in March 2022 when, in delivering his last budget statement as chancellor, that he intended to reduce the basic rate of income tax from 20p to 19p by 2024 (Parker *et al*, 2024).

Sunak asserted then that such a reduction would represent "a tax cut for workers, for pensioners, for savers" and, as noted, should the Conservative Party win the next general election, the basic rate of income tax would fall to 16p (*ibid*).

Undoubtedly amongst the headline grabbing changes made by Hunt last week was that national insurance (NI) will decrease by 2p meaning that Britain's 27 million workers will, on average, benefit by £450 each year.

Last week's cut in NI doubles the 2p cut previously announced by Hunt last November and which came into effect on January 6th.

As Sunak and his ministers undoubtedly hope, these changes will underline the party's traditional belief that lowering taxation is an incentive for workers and will underpin economic growth.

Nonetheless, as has been pointed out commentators, under the current government the 'overall level of taxation', which includes NI, VAT (value added tax), as well as all other taxes levied on property sales, holiday lets and companies, last year was the highest for more than 70 years (BBC, 2024).

And according to the Office for Budget Responsibility the independent body which provides oversight of the treasury's economic calculations, based on the predications made by Hunt and his team for last week's budget, "Tax as a share of GDP is forecast to rise to 37.1 per cent of GDP in 2028-29, 4.0 per cent of GDP higher than the pre-pandemic level" (OBR, 2024).

This would be the highest level of taxation since 1948 when this country was still reeling from the devastating impact of having dedicated phenomenal resources needed to fight in the Second World War that had proved ruinously expensive.

Hunt and Sunak will cite the fact that the UK's finances have suffered from unanticipated economic shocks caused by having to deal with the impact of a once-in-a-generation pandemic necessitating unprecedented lockdowns followed by Russia's illegal invasion of Ukraine resulting in energy prices spiking.

The need to spend hundreds of billions of pounds dealing with these crises, requiring a vast increase in government borrowing, resulted in the UK national debt, everything the government owes, increasing to some £2.65 trillion.

Expressed in figures, £2,650,000,000,000 represents 97% of the UK's gross domestic product (GDP), the total value of everything, goods and services, produced annually.

Though the government's main source of income is through the collection of taxes, such revenue is needed for day-to-day spending which makes debt reduction extremely difficulty (BBC, 2024a).

Though the current situation is a problem, it's not a new challenge.

Following the second world war, net debt was two and a half times greater than the size of the economy but, as investment was made in reconstruction combined with societal change and expansion of consumption, was progressively reduced to 21.6% by 1990-91. Net debt remained well below 40% until the global financial crisis in 2008 when the Labour under Gordon Brown intervened to provide urgent financing to a number of banks.

According to the latest data, £1,027 billion income was raised by the government in 2022-23, representing 40% of UK GDP highest this proportion has been since the 1980s (Keep, 2024).

Crucially, income tax, NI and VAT last year cumulatively contributed £591 billion.

Shortfalls in government finance caused by a deficit between revenue (taxes) and spending needed to provide sufficient finance to allow departments to function, are covered by the issuing of bonds, also known as gilts (United Kingdom Debt Management Office, 2024).

Gilts are issued for a fixed period, the average being is 14 years, and pay a 'coupon', interest rate, annually or semi-annually, that is a fixed percentage of their value, the 'principal' which is repaid in full at their expiry date (maturity). They are sold to financial institutions in the UK and abroad, such as pension funds, investment funds, banks and insurance companies.

However, gilts are internationally traded which, depending on the state of any country's economy, will cause their value to rise or fall which, when compared to the interest rate set when issued, will affect what's known as the yield.

This is important because, as explained in *Moneyweek*, the yield determines the rates for "mortgages, financial derivatives and can dictate government spending plans. They are essentially the foundations of the country's financial system" (Hargreaves, 2023).

Though the UK has a reputation as a safe economy, if indebtedness increases dramatically, their price goes down, the yield does up and, as a direct consequence, interest rates in general increase.

This is what happened immediately following the infamous 'mini budget' delivered in October by Kwasi Kwarteng as chancellor in Liz Truss' historically short administration.

As homeowners paying mortgages, especially those on variable rates of interest or coming to the end of a fixed rate deals know following the market turmoil caused by the mini budget, if the government is perceived to be spending without explaining how they intend to raise sufficient funds (taxation) to ensure debt does not increase rapidly, everyone gets clobbered.

This is the dilemma every chancellor and the government they are part of, must confront.

Accordingly, Hunt's pronouncements last week, particularly his insistence that government debt would reduce, was explicitly intended to give confidence to the money markets that the UK's finances are under control.

A key fiscal target for the government was that year-to-year borrowing should fall below 3% as a share of the economy in five years' time.

According to the OBR, this is likely to occur, and such borrowing will fall from £114 billion this year to £39.4 billion in 2028-29.

As the OBR also observe, net debt, and which includes that incurred by the Bank of England, is due to rise from 97.6% of GDP this year to 98.8% next year. However, though this type of debt will start falling after 2024-25 to reach 94.3% in 2028-29 (*ibid*).

Significantly, though, underlying debt, which excludes debt incurred by the Bank of England's activities, and the measure used by the government as it better reflects its policy decisions, won't fall until 2027-28, and then only by a mere 0.3% of GDP, £8.9 billion (*ibid*).

Notably, because Hunt's Spring Budget was nakedly intended to be part of a developing strategy the government hopes will reduce Labour's lead over the next six months prior to an election in October or November, what happens over the next five years becomes critical.

As is clear, the latest cut in NI, costing around £10 billion, will be achieved by an increase in taxes elsewhere including on vapes, business class airline users and those who are not domiciled in this country.

Among the criticisms that have been levelled at Hunt is that in introducing tax cuts for electoral gain, he's conveniently ignoring the key objective of reducing the size of the country's debt and, intentionally, kicking this problem into the next Parliament.

Worryingly, the question being asked is how the next government will, under the plans set out by Hunt, will be able to deliver public services (Conway, 2024).

Though Hunt stated that overall public spending will increase by 1% over the next five years, he also declared that the 'protected' services including the NHS, education and defence would receive much larger increases.

This is crucial as, unless more money can be raised, the logical consequence will be that all other 'unprotected' departmental spending would need to be reduced to keep within the rules any future chancellor would be expected to adhere to.

The Institute for Fiscal Studies, an independent think tank, believe unprotected departments would potentially have to cope with an overall reduction of up to £20 billion in the years 2024-29.

IFS director Paul Johnson believes what Hunt set out last week will pose "staggeringly hard choices" for the next government and that whoever becomes chancellor find themselves in the most difficult position "in 80 years".

Johnson added that as well as the vague commitment made by Hunt that, assuming the Tories win the next election, NI, which accounts for receipts to the exchequer of about £40 billion a year, could be abolished was "not worth the paper it's written on, unless [it is] accompanied by some sense of how it will be afforded".

Following publication of Hunt's budget, Johnson stressed what he considers to be a "conspiracy of silence" from both major parties in terms of how they plan to deal with tax and spending in the next Parliament.

The Resolution Foundation, which campaigns on behalf of families on middle and lower income, calculates that such cuts would amount to a reduction of in budgets of around 13% and, it stresses, as well as being inconceivable – "a fiction" – would increase poverty and division (2024).

Such a cut, it contends, would be equivalent to three quarters of the cuts suffered by these departments during austerity implemented by then chancellor George Osborne as part of the coalition government led by David Cameron to reduce UK debt needed because of intervention following the GFC.

Austerity in 2010-2015 is frequently cited as the reasons for the sense of being abandoned by many communities who perceived themselves 'left behind' by Westminster.

Pointedly, the perception of abandonment is cited by many commentators as having created the environment that led to many traditional Labour supporters voting to leave the EU in the referendum in June 2016.

Whatever the outcome of the next general election, the immediate prospects for many million is the feeling they're poorer than when they last voted in December 2019.

According to Paul Johnson in his IFS Post-Budget presentation, average household incomes this autumn will be likely to be lower than they were in autumn 2019, something he describes as "Not a happy prospect" (2024).

Any benefit that those in work receive from the reduction in NI – those with low income, particularly pensioners paying not paying this tax – will be likely to be worse off as worse off as they may be subject to 'fiscal drag' if their income increases and therefore pay more income tax (Chan and Penna, 2024).

Torsten Bell, chief executive of the Resolution Foundation asserts that the cuts in NI will benefit those earning between £26,000 or over £60,000, but that pensioners "face an £8bn collective hit" (Edser, 2024).

Thus, whatever benefit anyone receives from last week's spring budget are unlikely to be entirely offset by other measures that are "pushing up overall levels of taxation" (Partington, 2024).

The largest revenue generator will be the freezing of personal tax thresholds until 2027-28 which the IFS estimates will raise £44bn by the end of the freeze, £29bn having already been collected by April 2025 (*ibid*).

As the Resolution Foundation assert, the UK is “heading for nearly 20 years of lost pay growth as, after taking account of rising prices, the average wage will not regain its 2008 level until 2026” (*ibid*).

Crucially, it points out, if pay had continued to grow at the same rate as it had prior to the GFC in 2008 financial crisis, the average worker would have an additional £14,000.

The upshot of all this is that when people cast their vote at the next general election, they may do so in the full knowledge that their prospects have not improved since December 2019, quite the contrary (Rentoul, 2024).

Indeed, as the Resolution Foundation point out, many will feel their personal prosperity has got worse since the Conservatives replaced Labour almost 14 years ago in May 20104 and “This rising tax burden, alongside post-election spending plans, will leave a sour taste for whoever is in office [after the next election]” (Rawlinson, 2024).

There may be a variety of reasons why the Conservatives are so far behind in the opinion polls but, as the PM and his cabinet and advisors will know, voters tend not to support the party they feel has been instrumental in making them feel they’ve become less wealthy.

The Labour Party is unwilling to promise they will be able to radical solutions.

Shadow chancellor Rachel Reeves, interviewed on *BBC on Sunday*, explained that should Labour win the next general election, there’d be an immediate spending review but could not make any commitment public services would not suffer cuts (Uddin, 2024).

Intriguingly, Reeves has appointed a number of influential business leaders, including former governor of the Bank of England Mark Carney to be part of a taskforce to advise her on creating a National Wealth Fund with the objective of generating “billions of pounds in private investment to support the economy and rescue the party’s green energy plans” (Wheeler and Treanor, 2024).

Not everyone is convinced by Reeves’ strategy.

Guardian commentator Frances Ryan in her impassioned article, ‘What’s the point of Starmer’s Labour if it won’t stand up for poor, sick or disabled people?’ undoubtedly voices the view of many who believe that radical change is needed rather than simply “parroting Tory soundbites” (2024).

Significantly, and though I don’t expect Brexit to have the same significance in the next election as it did in the last (December 2019), our departure from the EU and the impact this has had on the economy cannot be ignored.

As seminal economics commentator William Keegan, who uses his regular column to stress his belief that leaving the EU, the world’s largest trading bloc, was an act of supreme financial self-destruction, contends the costs to the economy are already becoming apparent (2024):

“Hunt was a Remainer and fully aware of the self-harm, and indeed absurdity, of Brexit [and…] knows that anything up to £40bn (the Centre for European Reform estimate) may have been knocked off the “headroom” he has for budgetary concessions.”

Keegan believes matters will become progressively worse by citing predictions of the hit the UK economy will suffer by not being outside the EU; estimated to be a 5% reduction in GDP by Goldman Sachs and a 6% reduction by the National Institute of Economic and Social Research.

On the basis of these figures, the UK economy will be smaller each year by between £128 billion to £154 billion.

Though Keir Starmer would, if elected, seek to engage in more meaningful collaboration with the EU continuing Sunak's rapprochement following Boris Johnson's tenure when he engaged in confrontation for the sake of political expediency, though welcome, such "moves will not quickly deliver major economic change" (Shrimsley, 2024).

Among the considerable challenges the next government is likely to face after the election, will be the fact that as well as reducing this country's political influence amongst our closest neighbours, but is seriously undermining the UK economy and collective wealth.

That the UK's gross domestic product (GDP) grew by 0.2% in January (Butler, 2024), largely based on spending in the services sector, remains fragile and the immediate prospects for sustained recovery remain uncertain should make our political leaders more willing to think the unthinkable.

After all, providing leadership is supposed to be a vital component of their job description!

Steven's latest chapter, 'Boris Johnson, the green shopping trolley', was recently published in *Toxic News? Covering Climate Change*, edited by Mair, Ryley and Beck and published by Bite-Sized Books, London

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