Reboot for a new economy

Budget 2012: A budget for the 1%

Today's budget is another step in the wrong direction. Our economy is weak and the government is damaging its ability to recover with continued austerity and tax breaks for the wealthy.

Macroeconomic outlook

George Osborne was keen to claim economic forecasts supported the wisdom of austerity, particularly the UK's low interest rates at long maturities.

This is not the case**. Low government borrowing rates are not driven by confidence in the government's policies, but by quantitative easing**. £325bn of UK government bonds have now been purchased through QE, pushing down the yield. This has nothing to do with the government's fiscal policies.

In truth there is very little to be positive about:

- **Stagnant GDP:** GDP contracted 0.2 per cent in the last quarter of 2011. Most forecasters expect it will stabilise for this quarter, narrowly avoiding pushing the UK back into a technical recession. **Germany, the US and France have all recovered to their pre-crisis GDP levels.** The UK has not and shows no convincing signs of doing so in the immediate future.
- **High unemployment:** Unemployment remains the highest since 1995 with 2.67 million people out of work**. The youth unemployment rate is a staggering 22.5 per cent,** the highest it has been since comparable records began. Of those in work, 1.38 million are now working part-time because they cannot find a full time job.
- **Falling investment:** Investment by the private sector, the lynch-pin of any private-sector led recovery, after a brief uptick in the last quarter, is falling once more. It remains some £48bn below its 2008 peak. **Despite corporate tax breaks, large corporations are sitting on their retained earnings,** which have risen over the last 12 months in line with profits and are now at the highest levels since records began.
- **Trade Deficit:** The trade deficit rose in January, driven largely by falling demand from Europe. 40 per cent of UK exports are into the EU. The deficit had been closing somewhat until the end of last year, due largely to an approximately 20 per cent devaluation of the pound since 2007, rather than improved productivity or significant new investment.
- **Above target inflation:** Inflation remains significantly above the 2 per cent target at 4.8 per cent. The headline figure disguises much variation. The major effects of inflation for households will be felt in non-discretionary expenditure, like food and utilities bills.
- **Overwhelming debts:** Despite Osborne's claims, UK government debt, at around 64 per cent of GDP (excluding financial interventions), is not the UK's major economic problem. **The UK financial sector holds debt equivalent to around 600 per cent of GDP** – a chronic weakness that threatens further financial instability.

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Fiscal Policy

The lynch-pin of Osborne's economic strategy is the commitment to dramatic austerity, huge cuts to public spending to pay off the national debt. **270,000 public sector redundancies were made over the last 12 months**, with 600,000 expected in total (on OBR figures) over the course of the next few years.

In addition to the social costs of sharp reductions in public expenditure, this remains economically illiterate. Even a particularly dynamic private sector – the UK's is not – would find fighting against the effects of spending cuts increasingly difficult. In the case of the UK, it is a dead loss, and – while the effects are hard to quantify – the impact on confidence appears substantial. Surveys indicate that both business and consumer confidence remain very weak.

Taxation

Corporation tax

The independent Office for Budget Responsibility has exposed the Coalition's tax myths. Their new forecasts now show business investment growing by 6.9% *less* than previously expected over 2012, despite continual reductions in the rate of corporation tax.

Lavishing tax breaks on corporations is more than just unfair; it does nothing to deliver the new jobs Britain urgently needs.

High earners

The Chancellor argued that the 50p tax rate doesn't raise enough money to offset its 'damaging' effects. But there is no credible evidence that the 50p tax rate is harming the economy and even less to show the richest will create jobs.

The stamp duty increase on properties over £2 million is not a mansion tax; it's a one-off payment for the super-rich who are buying up prime property in London. Given most buyers are from outside the UK, these are not the same people that will win from a reduction in the top rate of tax.

Wealth for top 10 per cent is 100 times that of the bottom ten per cent, the rich are accumulating wealth at pace and this is widening both economic and social inequalities.

Low and middle earners

Increasing the Personal Allowance threshold to £9,000 is not as progressive as may seem. It will not benefit the poorest third in society, because they do not work or do not earn enough to be taxed at all, it will benefit middle income two-earner households most.

When the Personal Allowance threshold rises to £10,000, those earning between £8,105- £10,000 a year stand to benefit an extra £379 a year, a considerable increase in percentage terms. But in comparison with how much the richest 1 per cent stand to gain from changes to the top band (around an extra £50 per every thousand earned over £150k) this is of modest absolute value.

Missed Opportunity: The Green Investment Bank

The government has once again ignored the chance to invest in a new, sustainable economy. The Green Investment Bank was quietly side-lined despite the £3bn of funding promised by the government.

This is a serious mistake. The Chancellor should have announced an increase in its funding and an extension of its borrowing and credit-creation powers. Private investment has fallen by nearly £50bn since 2008 and shows no real signs of recovery. The Green Investment Bank should be beefed up so it can operate on a similar scale, to break the pattern of persistently low business investment in the UK relative to other G8 countries, and facilitate the UK's transition to a sustainable economy.

The UK needs an estimated £500bn of infrastructure investment over the next 10 years to replace aging and worn-out stock. Ernst and Young estimate that £162bn of clean energy investment is needed by 2025 to meet the UK's existing energy targets. The relatively small amounts in the GIB do not come close, while the Chancellor's attacks on green investment targets and cuts to subsidies help undermine investor confidence.

Read more about the economic alternative at:
www.neweconomics.org/reboot

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