

On-the-day briefing from **Edelman UK**

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Overview

Delivered in an economic climate far graver than the current government had envisaged, this year's pre-Budget report was, according to the Chancellor, the government's opportunity to show how it was acting to ensure that "the economic slowdown will be shallower and shorter than would have been the case".

Since its creation by Gordon Brown during his first year as Chancellor in 1997, the pre-Budget report has traditionally been the government's opportunity to outline its plans for the forthcoming Budget and to update its economic and budget forecasts. However, with the public increasingly concerned about recession and "economic crisis", and the government continuing to battle with a resurgent Conservative Party, the report's remit and political importance were far greater than any of its predecessors.

Described variously as a "mini-Budget", "emergency-Budget" and "economic recovery plan", the report was one of "action", announcing a £20bn "fiscal stimulus" and "substantial fiscal loosening", which included immediate tax cuts and an expansion of public spending aimed at providing a significant boost to the economy. Such bold political and financial measures fed into speculation that this year's report was "essentially an

emergency mini-Budget".

The report certainly appeared in stark contrast to the government's Budget earlier this year in March. As opposed to a Budget for "stability" and "competence" delivered with a noticeable lack of drama or rhetoric, today's report was described by the Chancellor as a "bold fiscal stimulus package" which aimed to "put money into people's hands".

The report has been described by commentators as a major shift in the government's economic policy, with the government believing that "significantly higher" borrowing is essential in withstanding and reducing the long term effects of an economic recession. As the Prime Minister stated in advance of the report "extraordinary times require extraordinary action." Indeed, the Prime Minister has closely associated himself with the report's success, stating that "To fail to act now would not only be a failure of economic policy but a failure of leadership. Doing too little too late would mean more damage and more deterioration." However, the opposition parties remain critical of the macroeconomic policies behind the report, believing that such an increase in public borrowing can only lead to a long-term increase in taxation.

Headline Points

This year's report took on a particular significance due to the recent background of economic uncertainty with all eyes and ears focused on how the government hopes to avoid the reality of recession becoming a prolonged slump. The Chancellor highlighted the "need for immediate action" with an announcement of a fiscal stimulus package worth £20bn:

- **VAT:** this will be reduced from 17.5% to 15% starting from Monday 1st December to last for 13 months (until the start of 2010).
- **Income Tax:** from April 2011, those with an income over £150,000 will have a 45% income tax rate.
- **National Insurance contributions:** these are to be raised by 0.5% from 2011.
- **Government Debt:** borrowing will rise to 8% of GDP by 2009/10, up to 57% of GDP by 2013-14 and this borrow-

ing is projected to decrease by 2015-2016.

- **Updated Growth Forecast:** Mr Darling says UK GDP growth this year as a whole is expected to be 0.75%. Output will continue to fall for the first half of next year. GDP is expected to fall to between minus 0.75 and minus 1.25% next year.
- **Banks:** closely monitoring banks' commitments to ensure lending facilities for firms are maintained.
- **Small Businesses:** Mr Darling announced a package of support for SMEs including a temporary increase in the threshold for empty commercial properties receiving tax relief and £1 billion support package for a Small Business Finance Scheme to provide business loans of between £1,000 and £1,000,000.
- **Fiscal rules:** Mr Darling confirmed the temporary suspension of the government's pre-set fiscal rules.

The Main Points

The Chancellor admitted that Britain would officially enter recession in 2009 - but he said it would be a “longer and deeper recession” without his actions. Britain faced “exceptional” economic circumstances and he wanted to take 'fair and responsible' steps to protect and support businesses and people now, while putting public finances on the right path for the future.

State of the economy

- **Economic growth:** The Chancellor conceded that growth in 2008 will be 0.75% and that the economy will shrink between 0.75% and 1.25% in 2009 - down from the 2.5% forecast in March.
- **Public borrowing:** Borrowing will rise in 2008-09 from a Budget projection of £43bn to over £78bn. In 2009-10, borrowing will exceed £118bn before starting to come down.
- **Budget:** The Budget will be brought back into balance by 2015/16, Mr Darling pledged.
- **Fiscal Rules:** As expected, Mr Darling announced a modification of the fiscal rules. It would be “perverse and damaging’ to stick to government borrowing rules in the current crisis, so they would be temporarily suspended.
- **The PBR represents a £20bn fiscal stimulus,** Mr Darling announced.
- **Public sector savings:** The Chancellor announced that a further £5 billion in efficiency savings would be found in 2010—2011.
- **Capital spending:** Mr Darling announced that the £3bn of capital spending will be brought forward from 2010/11. This will include spending on housing, schools and motorways.

The Environment

Due to the current state of the economy, environmental measures have inevitably taken a back seat. However, as was hinted by the Prime Minister in his speech to the CBI earlier today, the Chancellor announced proposals for more investment in energy efficiency.

- **Energy Efficiency:** The government will provide an extra £100m to help households improve insulation.
- **Air Passenger Duty** will be reformed into a four-band system ensuring those that travel further meet that cost.

Energy

- **Fuel Prices:** Ofgem will publish quarterly reports to monitor the link between wholesale and domestic energy bills. If the regulator identifies problems, the Government will use the law to force energy companies to pass on the benefit of falling wholesale prices to customers.
- **Road Tax:** The new vehicle excise duty bands announced in last year Budget will be phased in with the maximum increase next year to be £5 .

Personal Taxes:

- **Income Tax:** from April 2010, those with incomes over £100,000 will have their income tax personal allowance restricted and from April 2011, those with an income over £150,000 will have a 45% income tax rate.
- **10p Tax Rate Compensation:** the £120 compensation for those who lost out in the 10p tax rate issue has now been made permanent, and will rise to £145.
- **National Insurance contributions:** these are to be raised by 0.5% from 2011 for the employee, employer and self-employed.
- **Pensions:** the pension credit will increase from £124 to £130 a week for single people from April 2009. In the interim, there will be one-off £60 payment in the New Year.
- **Savings Taxation:** the government is rolling out the Saving Gateway scheme nationally from 2010 to encourage young people to save. The government will contribute 50 pence for every pound saved in scheme.

Employment

- **Strengthen pre-redundancy support:** Greater provision through the Train to Gain scheme, additional funding for JobCentrePlus and expansion of the government’s job advice service.
- **National Employment Partnership:** this brings together Government and major employers to tackle rising unemployment

VAT

- As widely expected, the Government grabs the headlines with a temporary 2.5% cut in VAT to 15% from 17.5% - the lowest level allowed under EU law - in hope of giving a boost to consumer spending.
- The cut will come into effect from December 1st and last until January 2010 with the Chancellor saying he would like retailers to pass on the VAT cut as quickly as possible. The VAT cut is the equivalent of a potential £12.5 billion stimulus to the economy.
- The relief will not, extend to fuel, where fuel duty will be raised to offset the VAT cut – the Chancellor arguing that fuel costs are falling substantially in any event.

Corporate Taxation

- **Deferral in Corporation Tax:** Small and Medium businesses will benefit from a deferral of the 1p increase in corporation tax.
- The Chancellor announced that from today, HRMC will allow firms facing difficulties to spread the timetable for paying taxes.
- Measures to help SMEs facing credit constraints include the creation of a Small Business Finance Scheme to support up to £1 billion of bank lending; a separate £1 billion guarantee facility to support bank lending to small exporters; a £50 million fund to convert businesses' debt into equity; and a £25 million regional loan transition fund to provide business loans of between £1,000 and £1,000,000.
- A further boost to small businesses, widely believed to have been pushed for by Labour backbenchers, is a temporary increase in tax relief thresholds for empty properties.

Child Benefits

- There will be an increase in Child Benefit from £18.80 to £20.00 per week for the first child from January 2009.

Housing

- More than £1bn to be made available to increase funding for social housing.
- Government to seek EU approval for a scheme that would provide guarantees for mortgage-backed securities.
- Lenders have agreed to wait three months after homeowners fall into difficulties before seeking repossession.
- Limit at which homeowners can apply for help with mortgage payments if they lose their jobs to be raised to mortgages worth £200,000.

Conservative Reaction



Victoria Barton
Senior Account Executive, Edelman
Former researcher to Andrew Mitchell MP, Shadow Secretary of State for International Development who worked in the Conservative Party

The Conservative Party continues to paint the picture of an irresponsible Chancellor and Prime Minister, who “did not fix the roof while the sun was shining”. George Osborne was on fighting form after various media reports and rumours that some of the Party faithful had been briefing behind closed doors that he was not suited to the job of Shadow Chancellor. Today was his chance to put such speculation to bed and he delivered a targeted message of “the tax time bomb” well.

The Conservative response focused on boom and bust and the tax bomb, suggesting that the measures the government has taken to ease the pressure across the economy are not sustainable, or in the best long term interests of the country. Rather, the government’s response is a politically motivated plan simply looking to the short term electoral win.

Adding to the message that Gordon Brown has been irresponsible, Osborne focused on the weakness of the UK economy. Stressing that the UK is in a weaker position than most European countries, he then went on to compare other European countries’ responses to the idea of cutting VAT. Osborne argued that the rest of Europe ruled out cutting VAT as it is thought that it would be difficult for retailers to pass on the benefits. This is something that the Conservative grassroots, as well as the general public, have noted, adding too that it will be very difficult to pass the 2.5% decrease on quickly and there will be a cost to retailers to implement the cut.

Osborne was also quick to question the Chancellor’s proposal to increase income tax to 45% for those on incomes over £150,000 a year. This will raise only £1 to 2 billion per year, not nearly enough to plug the spending gap. It is, according to the Conservatives, simply a distraction for the huge tax increases that will follow: the tax time bomb.

Labour Reaction



Luke Pollard
Account Director, Edelman
Labour PPC for South West Devon

Labour MPs have long been complaining behind the scenes that what they are looking for from the government is a policy that they can sell to their grassroots; a policy that speaks to the social justice agenda and sits happily in modern Labour thinking. In effect, a policy that will help people feel inspired to deliver more leaflets to aid their re-election. Mr Darling may have just pulled a rabbit out of the hat. The new top rate of tax, echoing proposals from the darling of Labour’s left, Jon Cruddas MP, brings much needed content to Brown’s new Labour narrative.

The changes in VAT will also be welcomed. Whilst not heralding a new consumer boom in itself the Treasury is signaling to hard pressed retailers that the government is ‘on their side’, especially as a 2.5% cut may be enough to psychologically encourage more people into the shops in the run up to Christmas.

Labour MPs will seek to pin the Tories down as the Party which has taken the wrong decisions for Britain by opposing the top 1% paying 5% more. This will play well to traditional voters and swing voters alike, who have been wondering where the quid pro quo for the bank bailout is going to come from.

Lib Dem Reaction



James Lundie
Director, Edelman
Former adviser to both Charles Kennedy and Paddy Ashdown

Liberal Democrat Shadow Chancellor, and new found national treasure, Vince Cable MP, has attacked the government’s Pre-Budget Report as tax ‘tokenism’. While welcoming the package of measures as far as they went, Dr Cable stated that the Liberal Democrat’s believed that consumer economic activity would be better stimulated by a permanent cut in income tax rather than a temporary cut in VAT. This, he stated, was welcome but would have a negligible effect.

The Liberal Democrats also attacked the government’s record in dealing with the banks who had taken public financial aid, claiming that the banks were still not lending to individuals and businesses in an acceptable way. Dr Cable said the government must “hold the banks to account”.

The Liberal Democrats will make income tax cuts for modest earners the main focus of their campaign structure in the next election.

The City's Reaction



Jonathan Smith
Associate Director, Edelman

Jonathan has advised UK, European and US businesses on financial and corporate communications for 10 years.

It was always going to be about confidence as Alistair Darling stood up to deliver his second, and much anticipated, Pre-Budget Report (PBR).

It was no coincidence that the global economic downturn took centre stage in the Chancellor's statement and was referred to as an 'unprecedented crisis' of our time. The restoration of financial stability was seen as 'crucial' to dealing with the crisis. The Chancellor related the UK's current condition to the wider global economic crisis and that the UK was in a position of 'relative strength' compared to other countries. This spreading of the blame was an under current of his speech.

The short-term solution according to the Chancellor was to give a fiscal boost of £20bn, around 1% of GDP. This will inevitably increase public borrowing on top of the effects of recession, but

will hopefully restore confidence and therefore growth towards the end of next year.

As expected short-term economic growth forecasts were slashed with the economy expected to shrink by around 0.75-1.25% in 2009. This was deemed to be a reasonable forecast for next year, but a more sceptical view was taken on the chances of achieving increased growth from mid-2009 onwards.

The Chancellor's optimism received an immediate mixed reaction from the City. The FTSE closed more than 9 pct higher after the PBR finished. The BBC's business editor Robert Peston put this down to the fact that the Chancellor was perceived to be addressing the issues head on and that his 'action' budget was better than doing nothing. Yet as Robert Peston went on to say, and he has a habit of calling the right tune on these issues, the view from the City today may be markedly different to the view from the City tomorrow.

Davis Buik from BGC Partners captured the mood in the city with his synopsis of the Chancellor's speech:
"Some good bits, some very bad bits. First and foremost the borrowing requirements for the next two years of £78 and £118 billion blew my brains away."

The Media's Reaction



Ben Burton
Senior Account Manager, Edelman
Ben spent four years as Meridian
Television's Political Correspondent.

The pre-budget report is always an important Parliamentary occasion but rarely does it develop such intense media speculation and attention.

Normally it's a chance for the government to tinker with a few elements and shine a light on their positive projections for the future – but this is a very different PBR in a very different time. The dramatic leaks or remarkable guesswork (depending on your viewpoint) from the country's Sunday papers proved accurate and took away the big surprises from today's announcement.

This means that journalists were on full alert throughout the Chancellor's speech for anything out of the ordinary that might have been slipped in. The 0.5% increase in National Insurance contributions from 2011 has caught the eye of most journalists

already looking at how it will impact those on middle incomes. Many reporters highlighted that whatever you think about the government's decisions this is an audacious plan to try and tackle the current economic situation.

Changes to the top rate of tax and the cut in VAT are obviously grabbing the headlines. Any more details about car tax, energy etc. will have to wait for tomorrow's newspapers. The focus this evening will be on the massive rise in government borrowing – increasing to a record £ 118 billion by next year.

"If he's wrong about a swift return to strong growth borrowing and debt will be much worse." Michael White at the Guardian says the government must be worried that so many factors are outside their control and the impact that could have on debt levels.

Tonight's news bulletins will try and spell out exactly what this unprecedented level of debt means for all of us. Will it work? Will we see more people splashing the cash in the run up to Christmas? We'll have to wait for tomorrow's front pages to see what Fleet Street makes of the government's proposals not to mention the political fallout.

More Information

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