Policy Exchange

"shaping the policy agenda"

The Budget 2011

Policy Exchange's response

Few surprises

There were few surprises in yesterday's Budget. The fact that it would be focused on growth has been well-known since the launch of the 'Growth Review' in November last year and the majority of the policies announced had been heavily trailed in the weekend newspapers. The fiscal picture does not change much – except for the downgrading of growth projections this year made up for by an improved forecast later on and a slight increase in net borrowing. This means that the Chancellor is still on course to eliminate the deficit by the end of this Parliament.

This is very good news. The biggest danger during a fiscal consolidation programme is that governments back down or water down their proposals due to political opposition or economic difficulties, as we extensively covered in our 2009 report, *Controlling Spending and Government Deficits*. The ratio we recommended of spending cuts to tax increases of around 80:20 is maintained. Spending is on course to be reduced to around 40% of GDP by 2015. This will help the long-term growth rate of the economy.

Areas of concern

While we believe that the Chancellor delivered a fair and balanced Budget, announcing a number of important and sensible policies, there are still areas that concern us. We have consistently argued that the best way to encourage growth in the UK is to let the market and entrepreneurs take the lead role, without the government trying to micro-manage the economy. We have argued that this would mean ensuring that government *allows* growth and does not try to *create* it. The Budget was some way from delivering this.

First was the sheer number of announcements. The Chancellor claimed to be scrapping 43 tax reliefs and reducing the number of pages of tax code by 100. But he then proceeded to replace this with 57 separate policy decisions. This, combined with the number of pre-announced policy measures coming into place after April 2011 (81), means that the economy will see 138 separate policy changes over the next five years. And that is without considering how many changes will come in future fiscal events.

Policy announcements were not only plentiful, but also complex. On tax there are complex interactions with income tax allowance increases and the shift to CPI uprating in future; estates are encouraged to give to charities in return for a 10% reduction in the inheritance tax rate; and the new "fair fuel stabiliser" sounds particularly opaque. Indeed the Chancellor had to read carefully from his script in order to get the detail right. For businesses a raft of extra money was announced – but much of this was targeted through allowances and incentive schemes that either apply to only a small sub-set of firms or are targeted at certain activities.

The combination of instability in tax and spending and continued complexity reflects the desire of government to "create" growth by targeting specific incentives at relatively small groups. In our view, it does not provide the clarity and certainty that businesses and entrepreneurs need to invest in our economy and this cannot be good for growth.

We also have concerns about the growth credentials of some of the specific policies. After being widely trailed, 21 areas will be made Enterprise Zones, where the government hopes that a simplified planning system and business rate discounts will encourage businesses to locate and grow there. However, with a total expenditure of just over £200 million over the next five years, the real question is why you would have zones when you can roll these sorts of policies out across the UK? Simplifying the planning system is a cheap and effective way to encourage growth everywhere – not just in small zones.

What would we have done instead? We outlined on Tuesday that our recommendations on planning reform and reducing regulatory burdens that the Budget took forward were just the start of what needed to be done for growth. We would have gone further to move towards a more collaborative and efficient planning system and to ensure that real reductions in regulatory burdens are delivered. One-in-one-out policies will only limit increases in regulation rather than reducing the overall amount; and by focusing on domestic regulation, the government is forgetting the massive burdens placed on firms by European regulation.

Going further in these areas will allow all firms, no matter what size, in which sector and no matter where they are located, to grow. It would allow the UK to develop better infrastructure and housing, both private and social, and to allow all parts of the UK to grow and see rising living standards. This is where we will be pushing further for reform.

Policy Exchange ideas implemented in the Budget

- As expected, the big giveaway for low earners was the increase in the income tax personal allowance. We commented in last weekend's papers that the previous approach to paying for this had been to bring more people into the 'Higher' rate tax and that a repetition of this would not be good for growth. We are pleased the Chancellor has not chosen this option. We believe that a tax system with a low rate and a wide base is optimal for growth – there will be opportunities to take this further with the proposed aligning of income tax and national insurance.

- The government is reforming its discount rate assumptions for public sector pensions. We have argued that the government's assumptions were no longer credible. The Chancellor also confirmed that that a public sector pension levy would be going ahead, as we advocated last year in *Controlling Public Spending: Pay, Staffing and Conditions in the Public Sector*. This is not only due to far more generous pension arrangements, but far more generous terms of pay, with an hourly premium of 35%.

- We are also happy to see the introduction of a fuel duty stabiliser, as recommended by our former Chief Economist Andrew Lilico as early as 2000. Further details on the creation of a Green Investment Bank – which we have advocated for some time – were also welcome.

- While, as we recommended in *Greener, Cheaper*, the Budget introduced a carbon floor price, the government's proposals have not gone as far as we recommended by concentrating solely on the electricity sector, and it has not (yet) included any attempt to counter carbon leakage, the increase in CO_2 levels in one country as a result of emissions reduction by a second country with strict climate policies. More work will be needed in this area.

- The announcement that businesses as well as local communities will be able to bring forward neighbourhood plans and development orders builds on ideas outlined in our recent report, *Making Housing Affordable*. This means that subject to agreement with the local community, they can develop plans without a need for additional planning consents. We were also pleased to see further detail on the scrapping of the 'national targets on development land'. This seems to end the requirement for councils to aim for 60% of new development on brown field sites, which made no sense for rural areas.

- The recommendation of the report, *More Homes: Fewer Empty Buildings*, that the government should reform the Use Classes Order to make it much easier to replace empty shops and offices to new homes, was announced by the government.

- A main recommendation of the report, *Making Housing Affordable*, argued the default answer to development should be yes rather than no – which the government is now enacting with a presumption in favour of sustainable development.

- The creation of further apprenticeships follows the course which we recommended in *Simply Learning: Improving the Skills System in England*. The government's willingness to support, rather than direct, business consortia marries with our notion that more apprenticeships should only be created where they coincide with a genuine demand in the economy, rather than on where central government deems the priority to be.

- The removal of taxes for non-domiciles for remittances purposed for UK investment will help prevent the exodus of high net-worth individuals who are particularly in danger of leaving in the financial services sector, as Policy Exchange pointed out recently in *Not with a Bang but a Whimper*.

- The Budget pledged to push ahead with Lord Young's review on reducing the burden of health and safety legislation, which was greatly influenced by our report, *Health and Safety: Reducing the Burden*.

About Policy Exchange

Policy Exchange is an independent educational charity. Our mission is to develop and promote new policy ideas which will foster a free society based on strong communities, limited government, national self confidence and an enterprise culture. In contrast to many other think tanks Policy Exchange is committed to an evidence-based approach to policy development. Our impact speaks for itself: from housing to policing reform, education to the NHS, our proposals have been taken on board by the main political parties. Registered charity number 1096300.

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