

Budget reaction: Sunak's Budget tries to delay the day of reckoning...but it is Coming

A personal view by Dr Stephen Barber

So much of Chancellor Rushi Sunak's second Budget was trailed in the press over recent days that it was any wonder he had anything left to say when he finally raised the Gladstone box and stood before the Commons on Wednesday. But amid the numerous measures announced and cash pledged - for everything from the Arts to sport to restart grants for small business, to an extended Business rate holiday, Free Ports and an Infrastructure Bank - is the broader question about the state of our economy. The Chancellor pledged to 'be honest' with people in announcing this Budget and the economic numbers outlined were as stark as they were eyewatering.

The recognition of this Budget is that while it might be delayed a little longer, a day of reckoning is coming.

As the Treasury analysis recognised, the experience of the past year and the deep recession we have experienced has a closer resemblance in some respects to wartime than the global financial crisis of more than a decade ago or indeed the great depression of the 1930s even though the contraction in 2020 surpassed both of these. The reach of the state into a private economy which has experienced a profound demand and supply shock is astonishing and has led to borrowing on 'an extraordinary scale'. The Chancellor announced an additional £65bn of measures to support the economy adding up to a total fiscal support of some £407bn this year and next.

The big 'surprise' announcement (if there was one) was the 'super deduction' for companies investing after Covid and allowing them to reduce their tax bills by 130% of cost. It recognises that not all business has suffered from lockdown and that the forced change in consumer behaviours has presented strategic opportunities to some just as it represented threats to many others. Many have been able to build up surpluses over the past year and this incentivises investment. The question that many organisations are (or should) be asking is to what extent will we return to the BC world and which are now permanent changes that require a shift in thinking? To what extent has this period changed the business environment for good?

Business has had to think and act very carefully about how to compete and survive during these months of lockdown. That intensity of thinking cannot let up as we eye the lifting of restrictions, not least because the Treasury is now signalling that its fiscal stabilisers will need to be taken off and before long. The OBR now expects a 'swifter and sustained recovery' to pre-covid levels of GDP than it had predicted back in November. This forecast

is optimistic for the economy bouncing back forcefully as it is reopened, reflecting the belief articulated by Bank of England Economist Andy Haldane that it is like a 'coiled spring'.

If the OBR and the Bank are right and there is as sharp a recovery as there was a downturn, then the Chancellor's job of plugging the hole that is a massive fiscal deficit, will be that much easier. But make no mistake, that fiscal hole is huge and will need to be filled in the coming years either with tax rises, a spending squeeze or both. This year the UK has borrowed £355bn or 17% of gross national income. The 'corrective action' this time centred on a freeze in personal tax thresholds, dragging more people into higher rate taxation, and an increase in Corporation tax to 25% in 2023. That increased tax on business profits is a political and economic risk for this government and expect some pushback. Also, given the worry, articulated by Sunak, that just a 1% increase in inflation or interest rates would cost the Treasury £25bn, expect a tighter fiscal rein in the years to come.

Sunak's promise to do 'whatever it takes' and direct fiscal firepower to protect jobs means that the furlough scheme and self-employment grants will be extended to the end of September (with additional employer contributions). But even with the billions of pounds spent to stave off redundancies over the past year, unemployment has risen by 700,000. His hope is that the extension until the autumn will give the economy just long enough to cushion job cuts and in doing so not to repeat the mistake of last year. But it is a leap of faith. The optimistic projection outlined in the speech expects the economy to be 3% smaller over next 5 years than it would have been and unemployment to peak at 6.5%. This remains a tough economic environment.

Business needs to be focused now on the economy to come, when state support is retracted, when the 'acute damage' is laid bare, when unemployment rises and when repossessions hit the headlines. Covid is still causing profound economic damage and recovery will be a long-term endeavour. Those with clear purpose and strategy will find opportunities but we cannot expect a simple back to business as usual.

This is a significant Budget. The Chancellor's initiatives from the super deduction to the Infrastructure Bank to Free Ports are all about boosting economic activity. But the truth is no one really knows how rapidly the economy will rebound and which sectors will prosper in the coming years. The day of reckoning is on the horizon – best be prepared.