Heartwood
Investment Management

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Investment Insight

UK Budget update

The end of austerity… or at least the promise of an ending?

On Monday, Chancellor Hammond welcomed an improved growth and borrowing outlook as he outlined the UK Treasury's latest Budget. In declaring that austerity was "finally coming to an end", the chancellor's rhetoric echoed Prime Minister May's claims at the recent Conservative Party Conference. Markets received the Budget quietly but constructively, with the UK stock market rising slightly on the day. Clearly, the Brexit issue will be much more of a market mover in the days and months ahead.

The chancellor also announced that national debt had peaked in 2016-2017 (at 85.2% of GDP) and was expected to fall each year for the next five years. Data from the Office for Budget Responsibility (OBR - the UK's fiscal watchdog) pointed to growth ahead, albeit not particularly robust, as well as sustained real wage growth in each of the next five years.

A better-than-expected UK deficit, bolstered by a tax receipt windfall, enabled the chancellor to use this Budget announcement to commit to increased spending on public services. This included an £84bn five-year deal for the NHS and better funding for mental health care, as well as an additional £1bn allocated for defence services. Education leaders, though, were disheartened to receive a one-off cash injection of £400m, which they perceive as inadequate for ongoing funding needs.

New taxes and old initiatives

Those expecting the chancellor to unveil efforts to bring the FAANGs (Facebook, Apple, Amazon, Netflix and Google) into line were not disappointed. In the event, this took the form of a new £400m 'Digital Services Tax' on the UK revenues of technology platform companies. The UK is the first country to introduce such a tax, though details on how it will be implemented (and its overall effectiveness) remain to be seen.

An increase in the personal allowance and higher-rate thresholds for income tax (to £12,500 and £50,000 respectively) has been brought forward by one year, to April 2019. Other major new taxes would have been challenging to secure without a Conservative party majority in the House of Commons, but a tax on single use plastic (a major pollutant) was introduced. The measure affects plastic with less than 30% recycled content, and is likely to receive significant public support.

The chancellor also abolished PFIs (public finance initiatives – whereby private firms are contracted on public projects) for all new infrastructure schemes, no doubt influenced by the damaging collapse of facilities management and construction company Carillion earlier this year.

The last Budget before Brexit

While Brexit received limited overt attention in the Budget announcement, the chancellor did claim that UK was well funded for its exit from the EU. The chancellor has long advocated cordial relations with the EU, and all OBR figures are based on a smooth Brexit, meaning that a no-deal Brexit could change the picture significantly. In that scenario, this Budget will become an irrelevance, and back to the drawing board the Treasury will go.

On the flipside, the chancellor has now optimistically pointed to the potential to harness "a double deal dividend" in the event of a smooth Brexit outcome. Ideally, this means that the economy would benefit from both an end to current uncertainty and the release of the financial buffer set aside to weather a chaotic Brexit, believed to be around £15bn.

The Heartwood Investment Team

Clear Thinking

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