AUTUMN STATEMENT 2022

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HUNT'S STATEMENT

Chancellor Jeremy Hunt delivered his Autumn Statement today following a turbulent few months in UK politics. The chain of events that led to this point was kicked off by Liz Truss's chaotic 'mini-budget' which announced large tax cuts funded by borrowing. This unfunded spree led to turmoil in the financial markets, the cost of government borrowing soaring and the value of the pound plummeting. The political fallout led to the collapse of her government, with Rishi Sunak coming to power with a mandate from Conservative MPs to restore the Party's economic credibility and the UK's international standing.

Hunt has comprehensively rejected 'Trussonomics' and embarked on the largest fiscal consolidation within the last decade, setting the political narrative and arguments leading into the next General Election (likely to be in mid-to-late 2024).

Whilst not a formal budget, the Autumn Statement represented one of the most important economic events in the last few years. Although Hunt has reversed almost the entirety of Truss's plans, the Chancellor has a huge task to repair the black hole in the public finances, caused by a cocktail of poor economic decision making, the post-pandemic recovery, and high inflation triggered by the war in Ukraine. Along with this, the Bank of England is predicting that the UK will enter an eight-quarter, or two-year, recession – the longest since reliable records began in the 1920s.

In order to address the situation, Hunt has introduced measures that he described as 'eye-watering' and 'difficult' - forced to bring forward both tax rises and spending cuts, to close the black hole at the heart of the public finances, whilst attempting to insulate the least well off from the economic headwinds. Hunt's stated focus will be on restoring stability, achieving growth and safeguarding public services.

This looks tough given the forecast from the Office for Budget Responsibility (the UK's economic watchdog) which predicts:

- A recession lasting just over a year from the third quarter of 2022, with a peak-to-trough fall in GDP of 2 per cent.
- Unemployment rising by 505,000 from 3.5 per cent to peak at 4.9 per cent in the third quarter of 2024.
- Real Household Disposable Income per person falling more than 7% over next two years, the biggest fall on record.
- Inflation coming in at 9.1% this year and 7.4% in 2023, falling sharply from the middle of next year.

Hunt's plans (as outlined in more detail below) are key to Conservative election prospects. He needs to turn the page on the last few months and develop a coherent narrative to sell the idea that a historic fifth term for the Conservative Party is something the British public can get behind.

With the polls still looking dire, that looks a tall order.

Key Areas

CLIMATE & ENERGY

One of the more positive announcements today concerns energy efficiency with £6bn of fresh funding for energy efficiency improvements. This funding will go towards establishing a new ‘energy efficiency task force’ tasked with reducing energy use in buildings and industry by 15% by 2030. The UK has a notoriously poor record on energy efficiency compared to its European peers so this funding will help to close the gap and improve resilience if the higher energy prices become the new normal.

In addition, Hunt announced the government would be going ahead with the new Sizewell C nuclear power plant, although it was widely pointed out that this project had already been repeatedly approved and as such was not a new commitment. Environmental groups also criticised the government for continuing to block new onshore solar and wind, which they claimed would unlock fresh capacity more quickly.

FOREIGN AFFAIRS

With Rishi Sunak’s views on foreign policy somewhat ill-defined, there has been interest in what the Autumn Statement means for the UK’s foreign policy.

The most eye-catching decision has been to maintain the UK’s international development spending at 0.5% of GDP, as opposed to the Conservative manifesto commitment of 0.7%. Given Jeremy Hunt and Andrew Mitchell (the new Development Minister) both rebelled on this reduction last year, the decision to break this commitment is even more remarkable. However, despite being unpopular amongst some MPs, given the most vociferous critics of this move are now in government, the decision is unlikely to garner a significant parliamentary rebellion. Lower development spending is also perceived within the party as one of the more popular spending areas to cut, and therefore an easy way to rake in additional funds.

Along with this, difficult spending decisions on defence have been kicked down the road. The government has confirmed that they will be refreshing the Integrated Review, the foreign policy strategy, and will await the outcome of that refresh before making spending commitments.

This means that spending will remain at current levels, deferring an argument between the Treasury and Ben Wallace, the Defence Secretary, who is an ardent advocate of higher defence spending. It seems unlikely that under Sunak, spending will reach the Truss commitment of 3% of GDP by 2030.

WHAT DID HUNT SAY?

Few Chancellors have had to present their first Autumn Statement in such extraordinary political and economic circumstances. Just eight weeks ago a Conservative Chancellor stood at the same Dispatch Box and told the country that tax cuts, especially for the wealthiest, were fundamental to growing the economy. Today, Jeremy Hunt, the fourth Chancellor this year, had to say that in fact tax rises were needed and that it was ‘fair’ that the wealthiest would bear the greatest burden.

In temperament and manner, Hunt is well placed to deliver the difficult news and reassure markets. To an almost silent House of Commons, he calmly set out that the UK is now in recession and the country needs to ‘face into the storm’ to find a path through it.

As with all fiscal statements the Chancellor’s speech attempted to address three audiences simultaneously - the markets, the public and his Parliamentary colleagues. The three priorities he set out - stability, public services and growth - were almost tailored to each audience individually.

To the markets, his mantra was credibility and stability. The pre-briefing and every word of the speech he delivered today, was intended to reassure that there is a credible path to deficit reduction and there were no surprises that could have unnerved the markets. Unlike his predecessor, he emphasised coordination with the Bank of England and the importance of monetary and fiscal policy working together. Today’s statement was the new Chancellor broadcasting again to the markets that this government is serious about fiscal responsibility, would respect financial institutions and earn back credibility.

To the public, however, Hunt was also trying to deliver a different message - this is not austerity 2.0. As well as being honest about the challenges, he said he wanted to be ‘fair about the solutions’. The widening of the highest rate of income tax, setting out the energy price guarantee extension, the retention of the triple lock and the increases to benefits in line with inflation, were all intended to support his assertion that the solutions to the fiscal challenge would not fall on those least able to cope.

This was also a Chancellor making clear that he is worried about both the deficit and inflation, but also the coming recession, and does not want to make it worse. In an attempt to prevent any overcorrection, public spending cuts he announced will primarily take effect after the next election. He also trumpeted small and surprise real term increases in health and education. This will appeal to the general public but markets may not consider that backloading the cuts to after the general election is entirely credible.

However, increasing the tax burden further will not be warmly received by Conservative MPs. Many will be critical publicly and privately of the Chancellor’s approach. Almost 8 weeks ago, nobody was speaking about tax rises and spending cuts, yet now the government has been forced into enacting them. MPs will be worried about the erosion of their dividing line with Labour.

THE LABOUR RESPONSE

‘Three Prime Ministers, four Chancellors, and four budgets later’, the British public is in a ‘worse place’ than we were 12 months ago. The Shadow Chancellor began her excoriating response to the Autumn Statement, demanding that the Chancellor should have come to the House asking for forgiveness, and offering an apology. Instead, she claimed the Chancellor has praised the strategy of his predecessor, and his ‘Kami-Kwasi budget’, serving the public with an ‘invoice for economic carnage created by the government’.

Highlighting the ‘Tory mortgage premium’ and ‘pensions in peril’, Rachel Reeves’s recurring claim was that the government has lost economic credibility.

For Reeves, the government are ‘pickpockets’, thieving from British working people with increases to taxes and double-digit inflation. Setting out some specifics of what the Labour Party would do differently and therefore her own dividing lines, she noted that, despite speculation, the Chancellor won’t be clamping down on non-doms, won’t apply VAT to independent school fees, and will retain tax loopholes for private equity managers.

The Labour argument is clear: ordinary people on low and middle incomes are paying the price for incompetent economic management and terrible Conservative decisions through falling real wages, higher mortgage rates, higher taxes and failing public services.

Concluding her speech, she told the House that the country needs a ‘serious long-term plan’ to grow the UK economy, putting forward Labour’s Green Prosperity Plan and Industrial Strategy.

This is no easy ride for Labour. The Autumn Statement will be painful for everyone and will involve difficult political choices for the government before the general election. But according to OBR forecasts, the public finances and people’s incomes will not be fixed until the late 2020s. Therefore, Labour will need to make tough decisions about what its offer to the British public will be in its manifesto.

KEY MEASURES FROM THE STATEMENT

- National Living Wage for people over 23 to increase from £9.50 to £10.42 an hour from next April.
- State pension payments, means-tested and disability benefits to increase by 10.1%, in line with inflation.
- Top 45% additional rate of income tax will be paid on earnings over £125,140, instead of £150,000.
- Income tax personal allowance, higher rate, National Insurance and inheritance tax thresholds frozen for further two years, until April 2028
- Local councils in England will be able to hike council tax up to 5% a year without a local vote, instead of 3% currently.
- Household energy price cap extended for one year beyond April but made less generous, with typical bills capped at £3,000 a year instead of £2,500. Benefit claimants and pensioners to receive direct cost of living support payments.
- Windfall tax on profits of oil and gas firms increased from 25% to 35% and extended until March 2028.
- Scheduled public spending will be maintained until 2025, but then grow more slowly than previously expected.
- In England, NHS budget will increase by £3.3bn a year for the next two years, and spending on schools by £2.3bn.
- Overseas aid spending kept at 0.5% of GDP for the next five years, below the official 0.7% target.
- Defence spending to be maintained at 2% of GDP – the NATO target.

WHAT DOES THE AUTUMN STATEMENT MEAN FOR BUSINESS?

What does this mean for business?

While businesses knew and accepted that the Chancellor would have to make tough fiscal choices on spending and tax to achieve market stability and control inflation, there was widespread agreement that not matching action on spending and tax with measures to tackle labour shortages and productivity would prove damaging in the short and long term.

The Chancellor is wary of the Conservatives' long-cherished mantel as the 'party of business', and in his opening remarks stressed that his statement would deliver stability. Today was about ensuring that the Conservatives are seen to be taking active steps to grow the economy and support business through these turbulent times.

To achieve this, the Chancellor was keen to put levelling up firmly back on the agenda, confirming that round two of the Levelling Up Fund will go ahead and HS2 funded as promised. He also committed to core Northern Powerhouse Rail and announced devolution deals for Suffolk, Cornwall and Norfolk – all critical for future business growth.

The Chancellor's announcement of a £13.6 billion package of support for business rate payers in England will also bring welcome relief. The multiplier will be frozen in 2023-24 while relief for 230,000 businesses in retail, hospitality and leisure sectors has also increased from 50% to 75% next year.

The Treasury had been in line to land a £3 billion windfall from the annual rise on business rates bills based on September's CPI inflation number of 10.1%. Ahead of today's statement, business groups warned that this would lead to retailers being forced to close stores in a further blow to the UK's high streets and called on the government to abandon or phase in the rise through transitional relief.

Briefed out in advance of today's statement, it won't come as a surprise that the increase in the energy windfall tax on profits earned by oil and gas companies will rise from 25% to 35% - raising £14 billion, including a new temporary 45% levy on electricity producers. Alongside this, Hunt announced the government's intention to maintain plans to spend £55 billion on the energy support package to assist struggling households and businesses. Although welcome news, business had been calling for longer term and wider support to survive rising inflation, staffing and running costs.

Initial reports suggest that the statement has failed to offer much cheer to markets, with both stock indexes and the pound all below their opening mark.

What's most telling (although not surprising) is that many of today's announcements relate to the years after the next general election – so some of the pain will not be felt for years to come, and quite possibly when we have a Labour government in post.

WHAT THE EXPERTS ARE SAYING

Paul Johnson, Director, Institute for Fiscal Studies: *"Simply staggering numbers in OBR report. Real Household Disposable Income per person to fall more than 7% over next two years. Biggest fall on record. Taking incomes down to 2013 levels."*

Ben Zaranko, Economist, Institute for Fiscal Studies: *"The OBR expect CPI inflation to be more than 7% next year. The Chancellor has confirmed he is sticking to his cash spending plans for the next two years, which are predicated on pay awards of ~2% per year. Another 5% real-terms pay cut for public sector workers on the way?"*

Ben Riley-Smith, Political Editor, The Daily Telegraph: *"Bulk of the spending cuts have basically been punted to after the next election. NHS and education actually getting more cash before then. Capital spending not cut. The squeeze then really pinches come 2025... when the Tories may not be in power."*

Torsten Bell, Chief Executive, Resolution Foundation: *"Conclusion? Jeremy Hunt has replaced Truss libertarianism with... what Labour could have announced:*

- *Tax: huge stealth tax hikes + visible raids on top*
- *Blair era people leading public service reform*
- *Spending: smaller day-to-day cuts than expected*
- *Loads of green rhetoric"*

Robert Colvile, Director, Centre for Policy Studies: *"£300 extra for pensioner households - why? Many pensioners are extremely wealthy. Why not means-test it? (Why not means-test all pensioner benefits?)"*

Marcus Johns, Research Fellow, IPPR: *"'You cannot borrow your way to growth,' is fundamentally untrue. It's cosplaying fiscal credibility but economically illiterate. Borrowing to invest is core to building strong economic foundations that deliver prosperity. We need to invest in our future #AutumnStatement"*

Sebastian Payne, Whitehall Editor, Financial Times: *"Quite the political pivoting by Jeremy Hunt - bringing in ex-Labour minister Patricia Hewitt to review NHS efficiency, Tony Blair's delivery chief Michael Barber for skills agenda, seeking "Scandinavian quality, Singapore efficiency" public services. Very New Labour/coalition."*

Paul Brand, UK Editor, ITV News: *"Boris Johnson promised to "fix" social care in 2019. Now Hunt says reform will be delayed by another two years, tho there'll be some extra funding. Three PMs in three years have all failed to deliver this central pledge. Meanwhile the care system slips into ever deeper crisis."*

Isabel Oakeshott, Political Commentator: *"This is an extraordinarily powerful Budget response from @RachelReevesMP and will make very painful listening for Tory MPs. A catalogue of extremely uncomfortable home truths...."*

THE POLITICAL ROAD AHEAD

The Tories look set to enter the next general election campaign, expected in Autumn 2024, off the back of 14 years in power, five Prime Ministers, a long recession, a sustained fall in living standards and a squeeze on funding for public services. Labour currently have a huge 22-point polling lead and that is before the measures announced today come into effect. This is not a favourable backdrop – so is a heavy Tory defeat inevitable?

The extraordinary volatility of UK politics in recent times should encourage a degree of caution, and the Tories have already demonstrated that low growth and austerity do not have to be fatal to their electoral prospects given that they won a majority in 2015 after the initial austerity programme under David Cameron and George Osborne. Although this was not a popular programme, the Tories successfully convinced enough voters that it was necessary, and that Labour's alternative economic policies lacked credibility.

So, can they pull it off again? Perhaps, although ironically, this time they will be looking to play up the global perspective whereas in 2010-15 they played that down in order to pin the blame for the fallout from the 2008 financial crisis on the then-Labour government. They will also hope that, with the economy set to return to growth in early 2024, they will be able to rely on a revised forecast from the OBR to ease some of the tax rises and spending cuts announced today just in time to change the mood music around the election.

However, the early indication is that voters are unconvinced; a recent YouGov poll found that 45% blamed the government's handling of the economy compared to 23% who blamed global factors. In addition, following the post-Brexit political realignment, the Tories have a different electoral coalition which is more exposed to the cold economic winds than in 2015. And, with a majority of voters now believing Brexit was the wrong decision, this could take one of the Tories' greatest electoral assets in 2019 off the table.

Nevertheless, Labour will resist any claims that they are strong favourites to regain power and they will continue to emphasise their own commitment to fiscal responsibility. The challenge for them will be to balance the desire for radical change – which attracted many new voters to the party under Jeremy Corbyn's leadership, particularly young urban voters – with the kind of more pragmatic prospectus that has traditionally been key to winning swing voters, particularly middle aged and older voters in suburbs and smaller towns.