Construction Equipment Association

UK BUDGET COMMENTARY AUTUMN BUDGET

October 2024

Published November 2024

Economics Professor Andrew Angus, from Cranfield University shares insight into the Autumn Budget and the impacts on the construction equipment sector.

The build up

The 2024 budget was perhaps the most important since 2010, when the coalition Government, led by David Cameron, set out its plan for governance. In 2024 it was the Labour Party, led by Kier Starmer, putting substance on its manifesto promises and it quickly became apparent that substantial tax rises were imminent.

Analysts generally agreed the Budget would try to raise £40 billion in tax revenue: £22 billion to fill a claimed “black hole” in government finances and £14 billion to deliver on Labour’s manifesto pledges “to fix the foundations” of the economy. As the scale of likely tax rises became apparent, the UK entered what PwC termed a “vibecession”, stalled growth, caused by bad vibes!

The Institute of Chartered Accountants in England and Wales found that their quarterly Business Confidence Monitor fell in Q3 2024, the first time in over a year. Consumers and businesses were postponing expenditure, waiting to see what the budget would bring.

While the country waited to learn which taxes would increase, it was almost certain that the budget would announce a substantial increase in government borrowing.Prior to the budget there had been very strong indications the chancellor would change the way that national debt was calculated, allowing more borrowing against the same fiscal rules. The scene was set.

The 2024 budget from a business perspective

The Chancellor, Rachel Reeves, delivered the new Government's budget on Wednesday 30 October 2024. The announcement revealed, as expected, a range of tax rises and borrowing to fund public services and investment projects.

There was scant good news for UK consumers and businesses. However, there was some. In a surprise move, the Government decided to scrap the freezing of income tax bands, known as fiscal drag, allowing employees to capture more of their pay rises. A welcome boost. Similarly, the chancellor was widely expected to increase fuel duty. Instead, fuel duty will be frozen for the 2025-26 tax year, bringing some relief to businesses and consumers.

Business bore the brunt of the tax rises in this budget, especially in relation to the cost of employment. The largest tax burden emerged as an increase to employer's National Insurance Contributions. The rate paid on these contributions will increase by 1.2% (from 13.8-15%) and the earning threshold will fall from £9,100 to £5,100 in April 2025. These changes could raise approximately £24 billion. Added to this, the Government accepted in-full, the Low Pay Commission recommendation that the minimum wage should be increased by 6.7% for those aged over 21 years in age, 5% above the rate of inflation (1.7%).

There were other notable changes to taxation on businesses beyond the construction sector. Starting from April 2026, agricultural assets worth over £1 million will receive an effective inheritance tax rate of 20%; starting in January 2025 VAT will be paid on independent school fees and the energy profits levy was increased from 35-38%.

Increased investment

By changing the way in which the Government defines debt, the Chancellor can borrow an additional £100 billion over the next five years. Added to the increased tax revenue, this enabled the Chancellor to announce a programme of significant public investment.

For many economists, this is a critical step for the UK economy. UK productivity, in terms of output per worker, has stagnated since the Great Financial Crisis and lagged other G7 countries. Improving productivity is key to economic growth, higher employment levels and higher pay. Many economists believe public investment in infrastructure is the key to unlock this productivity.

The construction sector will play an important role in this investment strategy. The Chancellor committed £5 billion to achieve the Government target of building 1.5 million new houses over the new parliament; £1.36 to increase the stock of affordable housing. Additionally, money was set aside for the recruitment of hundreds of planners to facilitate the building process.

Money was committed to the repair of buildings and infrastructure:

- £1.4 billion for school repairs and rebuilding.
- £1.37 billion into the removal of dangerous cladding from social housing.
- £500 million for road repairs.

In terms of transport, the Government has committed to the completion of the Transpennine Route and a link between Cambridge and Oxford.

There was insight into the new Industrial Strategy. This saw significant sums set aside for investment in what the Government perceives to be strategically important sectors. The budget committed £1 billion and £2 billion to the aerospace and automotive sectors respectively, tax breaks and some funding to the creative industries. The Government is also committing £20 billion to fund research in key areas of science technology, engineering and medical sciences.

The Industrial Strategy will also seek to catalyse green investments. The following commitments were made:

- £3.9 billion for carbon capture projects.
- £2.7 billion for nuclear power projects.
- £134 million to support offshore wind projects.
- £125 million towards the new GB Energy.
- £220 million for electric vehicle charging infrastructure.
- £1 billion in 2025 towards the warm homes plan.
- £1 billion to decarbonising the public estate.

The budget also ringfenced expenditure to invest in skills. The Department for Education has £950 million for capital expenditure, £300 million of which is for maintaining and improving further education facilities. There was £240 million for the ‘Get Britain Working’ scheme, which will tackle issues, such as getting those on long-term sick leave back into work. Further details will be published in an upcoming white paper. Also on the design table is reform of the Apprenticeship Levy, which will receive £40million.

Impact of the Budget

The dust is now settling on the Budget, impact assessments are emerging, businesses are planning how to cope with the increased tax burden. The various assessments point to a budget that will have short-term costs, with benefits emerging in the medium to long-term. Therefore, it may be several years until we can assess whether the Government's investment strategy has succeeded. However, some of the shorter-term impacts are becoming apparent.

Following the Budget, UK borrowing costs rose to the highest level in a year, as investors showed concern about the scale of borrowing and whether the planned investment would achieve returns. The increase in the cost of debt will be particularly important for the Chancellor. Currently, approximately £1 of every £12 spent by the UK Government is paying interest on debt. In 2023/24 interest payments on debt represented the 8.4% of Government expenditure. Any increase in this figure threatens to eat up some of the money the Government is set to borrow and squeeze out public and private investment. The pound's value has also decreased against the dollar.

A win-win solution to borrowing costs is to grow the economy, making debt smaller as a percentage of the size of the economy and making it more desirable for investors to buy UK debt. The Office of Budget Responsibility (OBR) expects the size of the UK economy, as judged by Gross Domestic Product (GDP), to receive a temporary budget fuelled boost of 0.6% growth in 2025-26, before fading, as the impact of tighter monetary policy, increased taxation and crowding out of private investment takes over. Overall, the OBR predicts economic performance to be the same as in previous forecasts before the Budget.

For businesses, the impacts of the NIC increase and new minimum wage presents near-term challenges. The IFS has produced some estimates of the impact of NIC increases, for a full-time employee earning:

- The minimum wage, companies will have to pay an extra £900 in NICs.
- The UK median income of £33,000, companies will have to pay an extra £770 in NICs.

Analysis by the (OBR) suggests that in the medium-term businesses will pass on 60% of the rise in the form of lower wages and higher prices and absorb 40%. As an aggregate effect on the economy the increase in NICs is expected to reduce the labour supply by 50,000 hours. The increase in minimum wage will be beneficial for workers, but it is likely to add £5-7 billion to payroll costs. With Labour's flagship Employment Rights Bill still to be released, there is likely to be further costs to come.

The anticipated increase in spending, funded by tax and borrowing, has had immediate bearing on the likelihood of an interest rate cut in December. While a cut in the rate of interest to 4.75% looks certain for November, many analysts were expecting a further cut in December. However, following the budget the likelihood of a rate cut fell. The expectation of higher government spending feeding through into inflation is likely to keep interest rates higher than they would have otherwise been. The OBR predicts interest rates will likely be 0.25 percentage higher over the next five years because of the budget.

Against these short to medium-term impacts, the OBR forecast that many of the planned investments will not deliver substantial gains until 2032-33. The long-term prediction is that these investments will add 1.5% to UK GDP by 2050.

The success of such long-term investment is hard to anticipate but will rely on a strong supply of skilled workers. This is particularly true of the construction sector, where latest figures show as a sector, there are many unfilled vacancies, relative to other sectors. A study by the Department of Education found that for the broader economy, 36% of all vacancies related to a skills shortage and that the UK has fallen behind its competitors in terms of training spend per employee, spending only half as much as European competitors. It estimates it will cost £6.5 billion to catch up. The budget goes some way to filling this gap, but still falls short.

Post-script

On Saturday 2 November, the Conservative party elected Kemi Badenoch as their leader. Focused on small Government and a strong private sector, this perhaps sets the stage for the coming years of UK politics. A Labour party focused on taxing and borrowing to pay for better public services and publicly directed investment strategies, versus a Conservative party focused on lower taxation, with fewer public services and an investment strategy led by the private sector.

As it stands, the UK has a Government that envisions the public sector taking a larger role in economic activity than the previous Government. It has put substantial onus on the private sector, to pay for public services. It has extended borrowing substantially, which will need to be paid for through further taxation and likely higher interest rates. Unless growth increases, which is not forecast for this parliament.

This is the gamble implicit within this Budget. The Chancellor has borrowed heavily against the future. This must deliver growth. The Industrial Strategy plays a key role in this. However, the Government has taken the role of deciding which sectors will benefit most from public funding. The real test of the 2024 budget will be whether the right sectors have been picked and the right investments chosen. However, it is likely to be some time before these judgements can be made.

Disclaimer: The opinions expressed are those of Professor Angus, an independent leading economist who spoke at the CEA Members' Forum on 30 October 2024.

CEA

For more information, please contact:

info@thecea.org.uk

(0)208 253 4502