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## UK BUDGET 2016 – NO GAME CHANGERS FOR GROWTH

### Berenberg Macro Flash

**No gamer changer:** Osborne delivered some nice reforms to boost businesses and help households. However, the cash shortage was also plain to see. The Chancellor announced a package of measures aimed at making the UK a better place for business, helping households save more, accelerating devolution within the UK and boosting productivity. But overall, the economic downgrades severely constrained the Chancellor's capacity to make significant changes. All in all, today's announcements probably do not mean much for the economic outlook.

**Economic downgrades were more significant than expected:** In the past, the OBR have been quite generous to the Chancellor when it came to forecasting the economy – not today. The OBR attributed the weaker economic outlook to: global growth, weak productivity growth in the developed world, high debt, deflationary risks, EM risks and financial market volatility – take a breath. As anticipated, investment and net trade were the biggest hit near-term but the OBR reduced GDP growth all the way out to the end of the forecast. Coupled with an improved labour market outlook in each year too, this indicates that the OBR's assessment of productivity growth and potential growth has fallen materially since November. As Chart 1 shows, the revised GDP forecasts are slightly above our own. The market volatility earlier in the year in addition to Brexit uncertainty will cause growth to slow in the first half of the year. Even with the downward revision in 2016 2.0%, in our view, risks to the OBR's near-term outlook are tilted to the downside.

**The Chancellor overstates the UK's policy buffer:** Today Osborne said "eight years ago, the UK was one of the worst prepared to face the financial crisis. Today, in the face of a cocktail of global risks, it is one of the best prepared." That is highly questionable. Whilst the UK is more flexible than most large economies, which would help it rebound from a crisis faster, it has far less cash to play with. It has the largest double deficit in the G7 (fiscal and current account). Similarly, just like almost everyone else, the UK has near-zero interest rates. In the event of a crisis, policy head room is far more limited now than it was pre-Lehman.

### Lot's of slicing and dicing as expected but the real surprise was the lack of Brexit talk

Despite the economic downgrades the numbers lined up in the end. The OBR still anticipates that the Chancellor will balance the budget in 2019-20 in line with the commitments in the Fiscal Charter. In the near-term, the projections for the deficit are broadly unchanged as Table 1 shows. But compared to November, the projected deficit falls quicker than expected in the middle of the forecast. Total debt as percentage of GDP will be 3.4 ppt higher by the end of the forecast. Increasing the pace of consolidation later down the road has enabled the Chancellor to save face today. However, it will probably come at the expense of missing the 2019-20 surplus target when the time comes. That is, unless the economy surprises strongly on the upside.

Where was the case for staying in the EU? Few days in the political calendar provide the Chancellor more airtime and attention than budget day. It was a surprise that he didn't slip in more arguments about Brexit and make his case for the UK to stay in the EU, apart from a reference to the OBR's view that a Brexit could cause 'disruptive uncertainty'. With the EU referendum just around the corner, this was an opportunity missed.



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**Conclusion:** Osborne announced some positive reforms and policies for households and businesses but no real game changers for growth. Most likely, it will be the OBR's downgrades to the economic outlook that will take the headlines today. In the end, the Chancellor achieved the key ask of the day. To keep the books balanced in the OBR forecast despite a challenging trilemma: an economy smaller and growing more slowly than a few months ago, fiscal consolidation only half way complete and his party in conflict over Brexit. Just getting the numbers to line up under these circumstances was such a big ask that it left little room for anything else. Key announcements were as follows:

### For households:

- Increase in the personal allowance to £11,500 and increasing the higher rate threshold to £45,000 by 2017-18
- Introduction of a new soft drinks levy
- Increasing the ISA limit to £20,00 as well as a new flexible ISA scheme for under 40's – save up to £4,00 per year and the Government will add 25%
- Help to Save for low income households – Government will top up 50% of upto £50 of saving per month

### For businesses:

- Cutting the rate of corporation tax to 17% by 2020
- Cutting the higher rate of capital gains tax from 28% to 20% and the basic rate from 18% to 10% from April 2016 (excluding residential property and carried interest)
- Abolishing Class 2 National Insurance
- Stamp Duty Land Tax reform
- Reducing the supplementary charge from 20% to 10% on the Petroleum Revenue Tax

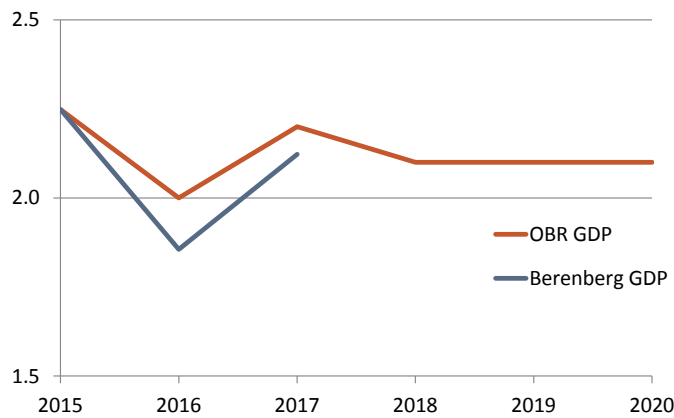
### Devolution measures:

- The opportunity for the West of England, East Anglia and Greater Lincolnshire to elect Mayors. As well as additional mayoral devolutions with Greater Manchester and Liverpool City Region
- Go ahead for High Speed 4 between Leeds and Manchester as well as additional funding to accelerate road improvements across the North of England
- Go ahead for Crossrail 2 in London

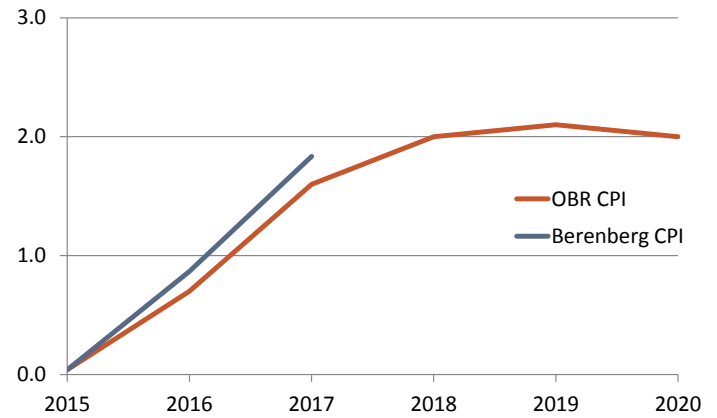


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**Chart 1: GDP outlook**

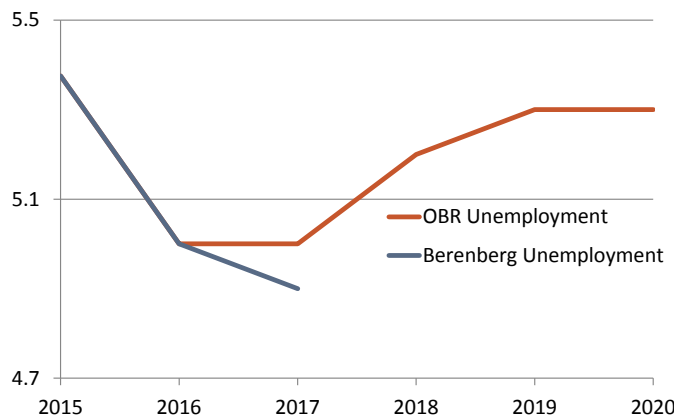


**Chart 2: Inflation outlook**



Source: OBR March Economic and Fiscal Outlook, Berenberg. GDP, CPI % yoy.

**Chart 3: Unemployment outlook**



Source: OBR March Economic and Fiscal Outlook. Unemployment % workforce.

<b>Table 1</b>		<b>2014-15</b>	<b>2015-16</b>	<b>2016-17</b>	<b>2017-18</b>	<b>2018-19</b>	<b>2019-20</b>	<b>2020-21</b>
General Govt. Deficit	Mar-16	5.0	3.8	2.9	1.9	1.0	-0.5	-0.5
	Nov-15	5.2	3.9	2.5	1.2	0.2	-0.5	-0.6
	<i>pp chg</i>	-0.2	-0.1	0.4	0.7	0.8	0	0.1
General Govt. Debt	Mar-16	83.3	83.7	82.6	81.3	79.9	77.2	74.7
	Nov-15	83.1	82.5	81.7	79.9	77.3	74.3	71.3
	<i>pp chg</i>	-0.2	1.3	0.9	1.4	2.6	2.9	3.4

Source: OBR March & November Economic and Fiscal Outlook, Berenberg