In Touch Technical Update

UK Spring Budget 2023

15 March 2023

For Professional Clients Only

The Chancellor has published the Spring Budget 2023, including the abolishment of the Lifetime Allowance and significant increases to the amounts individuals can save for pensions without being subject to additional charges.

Overall, the Chancellor has sought to alleviate key hindrances to long-term growth in today's Budget through changes in incentives against a still difficult economic backdrop.

At a Glance...

- The Chancellor focused on increasing long-term growth in his announcements by trying to address key issues, including in the labour market and lagging business investment.
- A key change is the significant increase in the Annual Allowance and the abolishment of the Lifetime Allowance entirely to encourage older workers to delay retirement.
- Otherwise, there were no other significant changes to taxation, whilst debt as a % of GDP is expected to decline by less than predicted in November over the 5-year forecast period.
- The OBR upgraded its growth forecast and still expects inflation to fall rapidly to below 3% by year-end. The economic backdrop remains difficult, however, and we continue to be cautious on the UK economy.

A Budget That Says *"We Need You Back In Work!"*

A key aim for the Chancellor today was to project stability and to avoid any semblance of a repeat of the much-maligned mini-Budget of last September — he seems to have achieved this. Beyond this, the press leaks and today's statement were clearly focused on trying to tempt people back into work and to incentivise more private sector investment — on fostering growth, in other words. On the former, whilst the UK's unemployment rate is near record lows, there have been concerning underlying trends, which have created acute labour market shortages in some sectors. These include an increase in the long-term sick and early retirements, which have been identified as an important hindrance to the country's growth prospects. The schemes announced today to try to address this include the large expansion to the government's support scheme for childcare costs to give parents of young children a better opportunity to return to the workforce, new training schemes and also important changes in pensions to try to persuade older workers to delay their retirements.

Important Pension Tax Changes

From 6 April 2023:

- The charge on benefits in excess of the **Lifetime Allowance** (currently £1,073,100) will be removed
- The **Annual Allowance** will increase to £60,000 (from £40,000)

The allowances to the left currently represent respectively the maximum pensions savings over an individual's lifetime and (broadly) the maximum pensions savings for an individual each tax year. Significant additional tax charges can currently apply where either of the allowances is exceeded. The changes will provide significant additional scope for tax-efficient pension savings.

The lifetime allowance (LTA) itself will be abolished in a future finance bill (expected to be effective from April 2024). Legislation links the maximum taxfree lump sum (the 'pensions commencement lump sum') to the LTA, this maximum lump sum will be frozen at 25% of the current LTA — so £268,275.

There is a lower annual limit that applies to money purchase contributions in tax years following the point at which an individual has "flexibly accessed" money purchase pension benefits. This **Money Purchase Annual Allowance** is also increasing from 6 April 2023 — from £4,000 to £10,000.

The highest earners are subject to a lower **'tapered annual allowance'**:

- Currently, those with 'adjusted income' in excess of £240,000 have their annual allowance of £40,000 reduced — by £1 for each £2 of 'adjusted income' in excess of £240,000, down to a minimum of £4,000 (where 'adjusted income' exceeds £312,000).
- From 6 April 2023, the taper works as above but starts from £60,000 at adjusted income of £260,000 and goes down to a minimum of £10,000 (where 'adjusted income' exceeds £360,000).

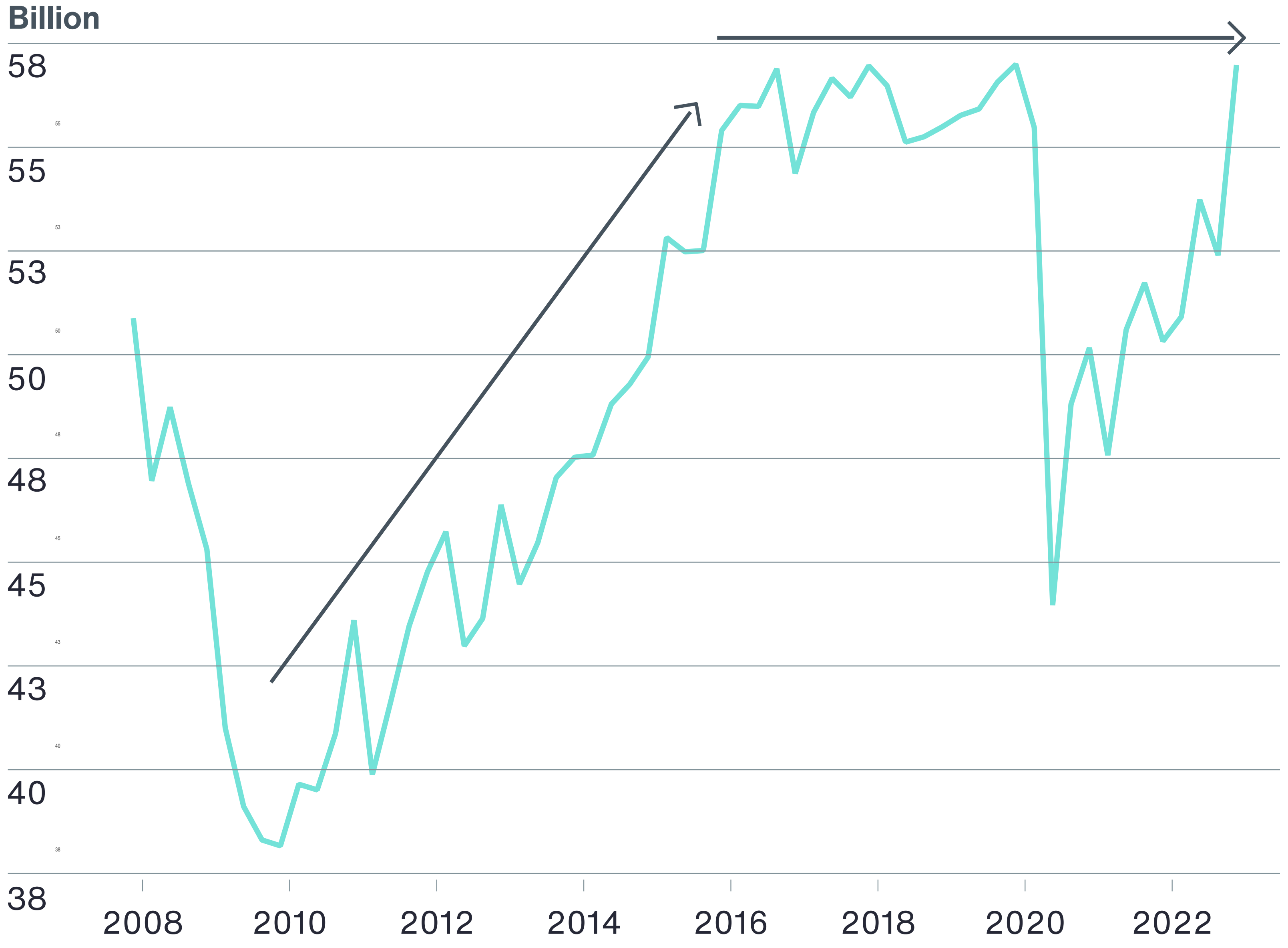
The 'threshold income' below which the tapered annual allowance can be ignored remains at £200,000.

A Budget That Says *"We Need You to Invest More!"*

Another key piece of the puzzle for Mr. Hunt is how to raise the UK's productivity and the trend rate of growth, which have been lagging since the global financial crisis. Policies introduced today include 12 new investment zones across the country, which offer tax incentives to companies, a review of the planning system for land use and a new set of capital allowances to help companies mitigate some of the impact of the planned rise in corporation tax from 19% to 25% on April 1. In particular, for the next three years, companies can fully expense any expenditure on plant, machinery and equipment against taxable profits. There were also increases to other allowances to promote R&D and small business investment.

UK Private Sector Investment Has Hardly Grown At All Since the Brexit Vote

UK Real Business Investment in GBP



Source: Macrobond

However, it could be said that the UK has been reeling from one crisis to another in recent years, which has made the environment for businesses highly uncertain and unpredictable, holding back investment plans. Today's incentives will likely be welcomed by the private sector, but we should not expect a material increase in business investment until the UK experiences a period of stability. Given the global backdrop, this seems unlikely in the near-term at least.

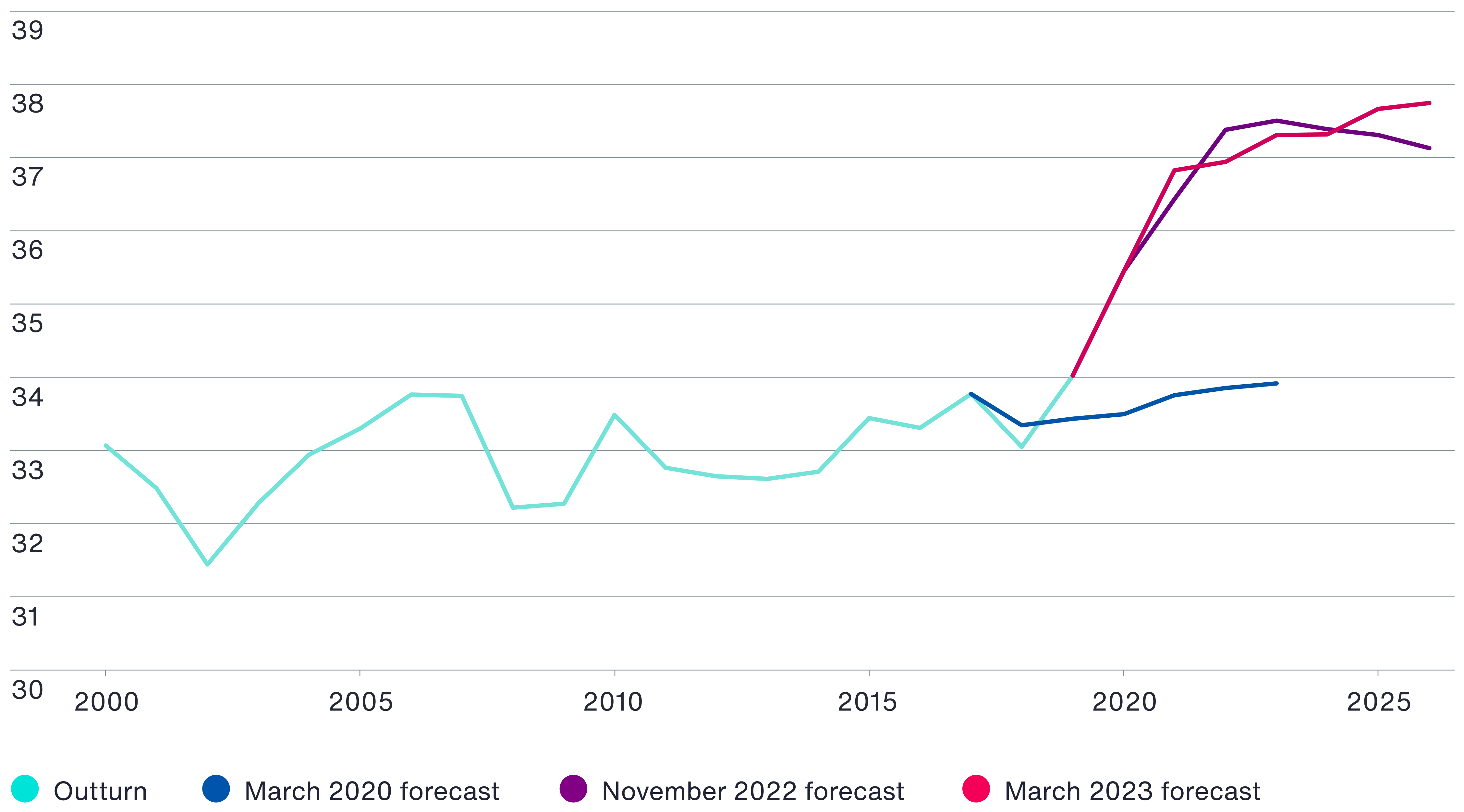
No Other Changes in Taxation

Aside from the changes in the pensions tax allowances, there were no other major changes to personal or business taxes. Given the events of last year — large tax cut announcements followed by a massive U-turn — it was never likely that the Chancellor would tinker further here. The net result is that the UK's tax burden (tax as a share of GDP) is set to continue rising over the next 5 years to almost 38%, which is greater than forecast in November and clearly its highest since the Second World War.

As a result, today's changes in incentives will need to work against the government's imperative to stabilise deficits and debt over the forecast horizon. It also implies that the government will find it difficult to stimulate the economy in any significant way in coming years.

The UK Tax Burden Set to Keep Growing

National Accounts Tax % GDP

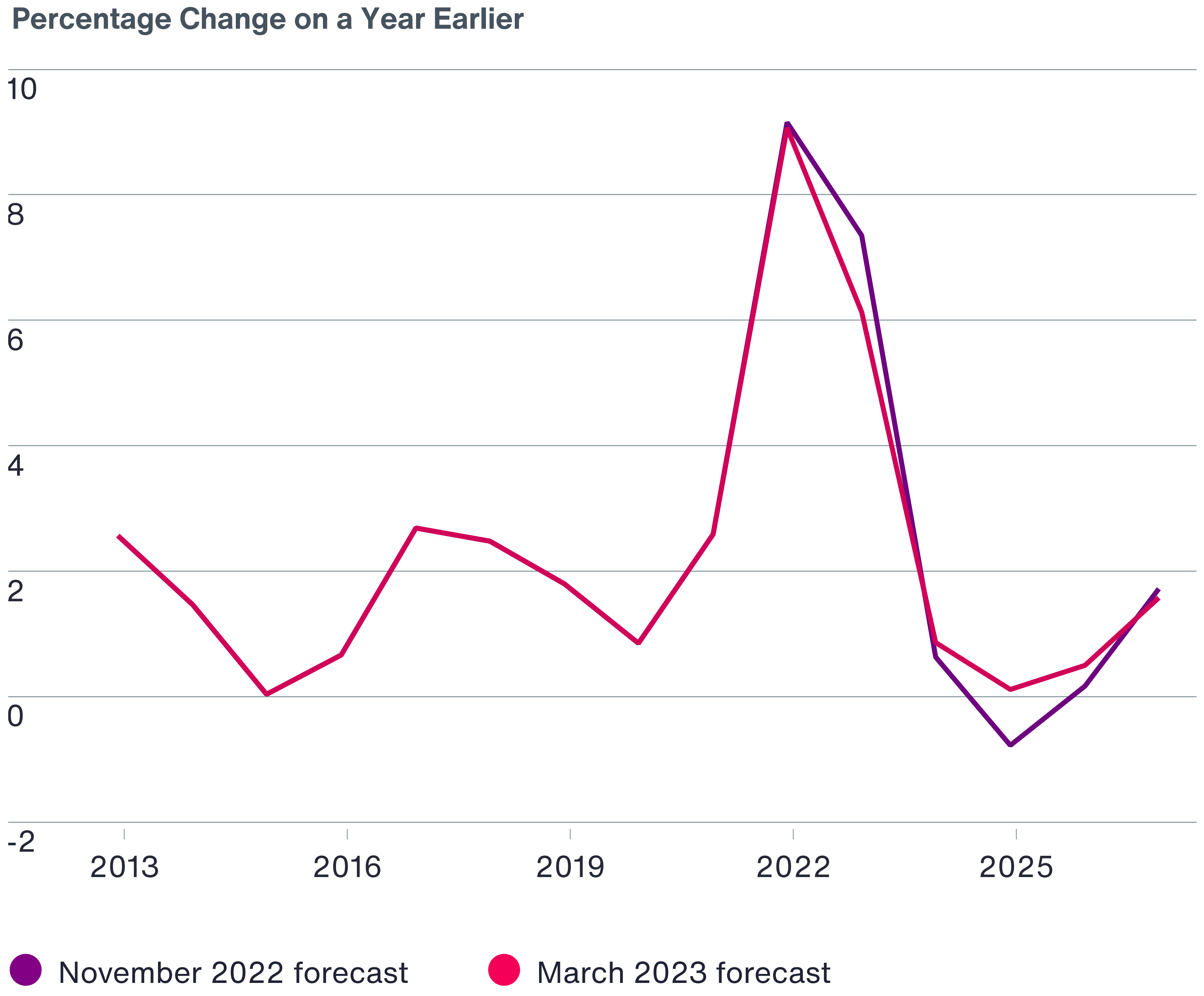


Source: OBR

Economic Forecasts Revised Up but Backdrop Remains Difficult

Additionally, the Office for Budget Responsibility's (OBR) updated economic forecasts for UK reveal a small upward revision to growth, removing the previously predicted technical recession from the forecasts, while inflation is still expected to decline sharply in the coming year, albeit by a little less than previously thought. In terms of real GDP growth, the economy is still expected to decline by 0.2% this year and to grow on average by 2.1% over the subsequent 4 years.

Inflation Forecast to Fall Very Rapidly This Year and Stay Close to Zero until 2026



Source: OBR

Meanwhile, inflation is expected to fall to 2.9% by the end of 2023 and to average less than 1% between 2024–25 and 2027–28. Despite some upward revision to the inflation forecasts, this is still an especially low estimate for inflation in our view and vulnerable to the considerable uncertainty we still see in the coming years.

Overall, this remains an especially difficult backdrop for policymaking and goes a long way to explaining the lack of tax cuts in today's budget. This is despite the fact that this will be one of the last chances for the government to influence the UK's economic performance before the next General Election, scheduled to be held no later than January 2025.

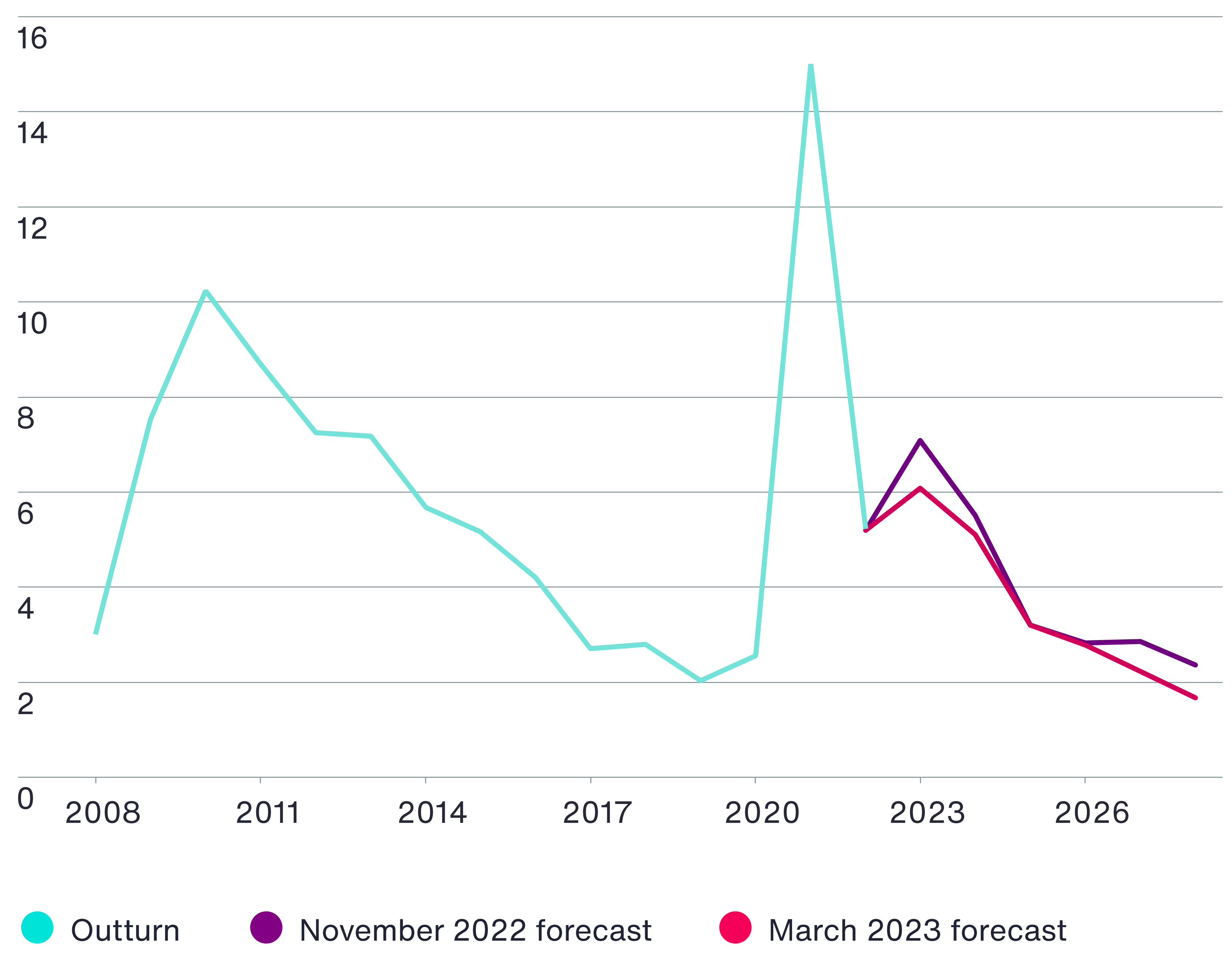
Debt and Deficits Forecast to Fall Gradually From High Levels

Higher than anticipated inflation, lower energy costs and a relatively resilient economy have combined to improve the fiscal outlook, hence today's announcements on the energy price guarantee extension, childcare and pensions. However, it still remains the case that the impact of the past few years' crises will linger for many years to come.

The deficit (the Public Sector Borrowing Requirement) is now forecast to fall from its current level of over 6% of GDP to 1.7% by 2027–28, while public debt is seen to be falling to 96.9% of GDP. The latter is higher than the November forecast and the highest since the early 1960s. In terms of Gilt issuance, the Debt Management Office (DMO) has reported that its Net Financing Requirement in the fiscal year 2023–24 is forecast to be £246.1bn, financed by gilt sales of £241.1bn and net Treasury bill sales of £5bn. In terms of the split, 36% of sales is planned to be in short duration Gilts, 27.1% in medium duration and 21.1% in long duration Gilts. Index linked Gilt sales are planned to be 10.9% of the total.

The Focus on Bringing Debt Down Will Continue

National Public Sector Net Borrowing % GDP



Source: OBR

Contact Us

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