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A free market take on the 2012 budget [1]

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Generally positive on tax?

? Cutting the 50p tax rate to 45 percent is a step in the right direction, but the Chancellor should have scrapped this altogether. The danger is that the 45p will become a permanent rate. The government should commit to scrapping this new top rate tax before the next election.

? Raising the personal allowance to £9,025 is also very welcome. The government should raise its target from £10,000 to £12,400, which would lift minimum wage earners out of tax altogether.

? The government?s commitment to merging income tax and national insurance is very encouraging. Britain?s tax code is absurdly complex and tax simplification should be one of the government?s top priorities.

? The ?tax receipt? idea could make a big difference. By making spending more transparent, people will be better able to hold the government to account for its fiscal policies. With a bit of luck, these tax receipts could sow the seeds of a small government revolution as more people realise how wasteful government spending really is.

? The additional cut in corporation tax is a good, pro-growth measure that will boost Britain?s economic competitiveness. But it should go further ? competing with large countries is not enough anymore, and a corporate tax rate higher than 20% is still too high. Furthermore, the new and/or expanded allowances and tax credits the chancellor announced will increase complexity and run against the general theme of tax simplification.

But there are a few negatives on tax too?

? Raising tobacco duty by 5% above inflation is petty, vindictive, and possibly self-defeating. Such taxes are already extremely regressive, hitting the poorest the hardest. Moreover, high levels of tobacco duty are already encouraging smuggling and counterfeit cigarettes. Cigarette smugglers will be very pleased at today?s duty hike.

? Reducing the 40p rate threshold will mean that only basic rate taxpayers will benefit from the personal allowance rise. Up to 300,000 people will now find themselves upper rate taxpayers as a result. This will hit single-earner families particularly hard.

? The General Anti-Avoidance Rule is a bad idea. It leaves far too much latitude for bureaucratic discretion. It adds another layer of complexity on our labyrinthine tax code. And it is an affront to the rule of law. Radically simplifying taxes is a much better way of ensuring people pay their fair share.

? Raising Stamp Duty Land Tax on homes worth more than £2m is a politically-motivated sop to the Liberal Democrats. Taxes like stamp duty are damaging because they discourage transactions and gum up markets. They also raise very little revenue.

The budget is weakest where it strays into industrial policy?

? Was the tax credit for animation, video games, and high-end TV production designed just so the Chancellor could make his ?Wallace & Gromit? joke? These are unquestionably attractive, wealth-creating industries, but the government should not be picking winners and advantaging politically-favoured businesses over less fashionable ones like this.

? In promising to fund superfast broadband in 10 British cities, the government is creating a role for itself where it just isn?t needed. Over the past two decades, the private sector has delivered (and continues to deliver) a vast digital infrastructure at virtually no cost to the taxpayer. It is hard to think of a better example of something the state should simply stay out of.

? The Chancellor?s call for increased airport capacity in the South East is a good thing, but it is worth remembering that the politically-motivated rejection of such airport capacity has been explicit government policy up until now.

? The various credit, business, and construction support schemes contained in the budget are misguided, and will do little except preventing markets from adjusting to changed economic circumstances, as they must if we are to return to robust, sustainable growth. Nevertheless, these schemes are probably small enough to be dismissed as pointless gimmicks rather than serious market distortions.

The macro outlook is worse than the chancellor is letting on?

? The growth forecasts the chancellor announced still look implausibly optimistic. The public sector, financial industry, and housing/construction sectors all boomed unsustainably in the 2000s, and must probably contract further as the economy rebalances. We are weighed down by debt, and the deleveraging process has barely started. So in the absence of significant and radical supply-side measures to boost growth in the rest of the economy, it is hard to see how these forecasts can be met. And that?s before you even consider the sizeable downside risk posed by the eurozone crisis and our still-fragile banks.

? The government?s borrowing costs are low not because of the chancellor?s fiscal rectitude, but rather because the Bank of England is directly intervening in the gilts market to reduce borrowing costs via quantitative easing, and because things in the eurozone are even worse than in Britain. The economy may be getting better, but the overall macro-economic picture remains far worse than the chancellor is likely to admit.

? Finally, it is worth remembering that for all the talk of austerity Britain, the government will still borrow £126bn this year. That?s £14.5m an hour, every hour, all year long.

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