Budget 2013: The good, the bad and the ugly [1]

Written by **Sam Bowman** [2] | Wednesday 20 March 2013

It?s not saying much, but this was George Osborne?s best budget yet. These tax cuts are long overdue, though they are not significant enough to solve Britain?s growth problem. Cutting taxes for businesses will stimulate investment and job creation, and reducing the tax burden for low- and middle-income earners will make life easier for them.

But government spending is still rising by £20bn this year. The government?s plans to meddle in the housing market are staggeringly misjudged, and we risk repeating exactly the same policy mistake that led to the US subprime mortgage bubble. And we?re still going to be borrowing £108bn this year ? that?s £295m a day, every day, with no end in sight.

The Good

Personal allowance raised to £10,000 by 2014. Income taxes are smothering workers. The taxman takes more than 30p out of every pound earned by low- and middle-income workers above the personal allowance. Raising the personal allowance to £10,000 ahead of schedule is a significant step to reducing the tax burden for low- and middle-income workers, and creates the tantalising prospect of the personal allowance being pegged to the minimum wage rate in 2015.

Corporation tax to be cut to 20% by 2015. At last, an encouragingly bold tax cut for business. The corporation tax rate will be falling from 28% to 24% this April, then from 24% to 21% next year, and finally from 21% to 20% in 2015. Although this does indeed put Britain ahead of other ?major economies?, small countries like Ireland (which has a corporation tax rate of just 12.5%) will still be able to outcompete Britain in attracting investment from multinational corporations.

Employers? national insurance bills cut by £2,000 for every firm. Employers' NICs are a direct tax on jobs, so tax relief should allow some businesses to take on extra employees. The cut will have the most pronounced impact on micro-businesses, 450,000 of which will reportedly be taken out of tax altogether.

Beer duty to be cut by 1p, and the ?beer duty escalator? to be scrapped. Two weeks ago the government was pushing for minimum alcohol pricing, and now it?s cutting the price of beer. It might not be cutting duty by much, but it?s a welcome change after years of miserable, anti-poor paternalism. And scrapping the outrageous ?beer duty escalator? is long overdue. No Chancellor should be able to pretend that a tax hike is out of their hands.

The Bad

The Bank of England?s 2% inflation target to stay in place. Inflation targeting has failed. It creates invisible

excess inflation during boom periods (by keeping prices rising by 2% when prices should be falling because of productivity gains) and cannot offset changes in velocity in bust periods, leading to secondary deflations that amplify the damage caused by the initial bust. An alternative, rules-based system (such as an NGDP target based on a futures market instead of the discretion of the Monetary Policy Committee) would be a much less harmful mandate for the Bank of England. Mark Carney had indicated that he was sympathetic to this kind of reform. By giving up the chance to rethink British monetary policy, the Chancellor has snatched defeat from the jaws of victory.

20% tax relief on childcare vouchers up to £6,000 per child from 2015. Expensive childcare is a consequence of the costly regulations [3], such as mandatory maximum children-to-staff ratios (3:1 for under-5s and 1:1 for infants under one year old). If the government wants to make childcare more affordable, cutting these sorts of regulations back would be a better place to start than using taxpayers? money to pay for childcare for parents earning up to £300,000/year.

Tax avoidance and evasion measures aimed at recouping £3bn in unpaid taxes. Tax avoidance is a legal and legitimate response to the perverse incentives of a complex tax code created by politicians trying to exempt a pet project or special interest that they favour. Tax evasion, too, is a rational response to high taxes and is only possible because of the complications in our tax code. The best way to reduce evasion is to simplify the tax code, not to persecute people taking advantages of a corrupt system.

£3bn extra for new projects every year from 2015-16 until 2020, totalling £15bn. Capital spending projects are always popular with politicians who want to leave a expensive railway line, bridge or motorway as a legacy, but there is a long history of infrastructure projects doing little help their flagging economies. Barack Obama?s $800bn stimulus package, launched in 2009, focused on ?shovel-ready? projects and did virtually nothing, as did successive Japanese stimulus programmes in the 1990s and 2000s. Any extra money from spending cuts should be given back to the private sector through tax cuts, where it can do the most good.

?and the Ugly

Bank guarantees to underpin £130bn of new mortgage lending for three years from 2014. Apparently the Treasury has not learned the lesson of 2008: injecting taxpayer money into the housing sector will simply inflate prices, distorting price signals and stoking the housing bubble that already seems to be growing in the housing sector. Houses are expensive because supply is restricted by the planning system. Instead of throwing money at the problem and driving prices up even more, the government should have the courage to liberalize planning to allow more development, including on green belt land.

Government ministers picking winners. Fiddling with tax breaks for specific industries is a mug?s game. There is no way the government can know which industries to promote, and these projects inevitably collapse into a mess of overcomplicated grant schemes and politics-driven bailouts of failing firms. Only consumers can pick winners.

Government spending is still rising. Despite all the talk of cuts, the government will still be spending £761bn this year, nearly £20bn more than last year. By leaving healthcare alone and failing to carry out the big structural reforms needed to reduce social security spending, the government is not matching its rhetoric on spending with the action needed. We?re still going to be borrowing £108bn this year ? that?s £295m a day, every day, with no end to the borrowing in sight.

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