Brewin Dolphin

Spring budget 2023

15 March 2023

Chancellor Jeremy Hunt has delivered his spring budget, in which he set out plans that aim to boost UK economic growth, while being mindful of the need not to spook financial markets.

With the fallout from his predecessor's mini-budget still fresh in people's minds, Hunt did not announce any significant tax cuts for households. Instead, this spring budget[1] focused on incentivising people to re-join the workforce and remain in work for longer. This follows a jump in economic inactivity since the pandemic, which has been largely driven by an increase in early retirement[2]. Hunt announced that the pension lifetime allowance will be abolished, and the pension annual allowance will rise to £60,000. Free childcare for working parents will be extended to cover children from nine months old, while over-50s will be offered "returnerships" to help them retrain and get back into the workplace.

Other announcements included some limited support for households struggling with the cost-of-living crisis, the confirmation of an unwelcome tax hike for businesses, and measures that aim to incentivise business investment.

Here, we highlight the key announcements, before giving Guy Foster's view on the implications for the UK economy and investors.

Lifetime allowance abolished

In an unexpected move, the chancellor announced that the lifetime allowance – the amount of money you can build up in pensions without triggering a tax charge when you come to access pension benefits – will be completely abolished. From 6 April, savers accessing pension benefits in excess of the lifetime allowance will no longer face a tax charge of up to 55% on the excess.

This is an extraordinary change of direction. The lifetime allowance was introduced in April 2006, when it was set at £1.5m. It reached a high of £1.8m in 2010/11, was slashed to a low of £1.0m in 2016/17, before three increases brought it to its current level of £1.07m[3]. In April 2021, prime minister Rishi Sunak (who was chancellor at the time) said the lifetime allowance would be frozen for five years until 2026, but Hunt's announcement means this will no longer happen.

Abolishing the lifetime allowance is one measure that aims to deter people – especially doctors – from reducing hours or retiring early because of potential tax liabilities. The number of people paying tax charges as a result of breaching the lifetime allowance rocketed by 578% from 1,270 in 2011/12 to 8,610 in 2020/21, according to HMRC. After 6 April, savers will no longer need to worry about these tax charges.

The change doesn't mean that future retirees will be able to draw more of their pension savings as a tax-free lump sum. The 25% tax-free lump sum is currently capped at £268,275 (namely, 25% of the current lifetime allowance) and the government has announced that the cap will remain and be frozen at this level.

Annual allowance increased to £60,000

The standard pension annual allowance – the maximum amount you can save into pensions in any one tax year without having to pay a tax charge – will be increased from £40,000 to £60,000 from 6 April. In other words,

1. https://www.gov.uk/government/publications/spring-budget-2023
2. https://committees.parliament.uk/committee/175/economic-affairs-committee/news/175197/early-retirement-and-our-ageing-population-are-causing-labour-shortages-says-lords-report/
3. https://www.gov.uk/government/statistics/personal-and-stakeholder-pensions-statistics (table 8)

savers will be able to pay up to £60,000 or 100% of their UK relevant earnings (whichever is lower) into pensions each year and benefit from tax relief.

The annual allowance was introduced in April 2006, when it was set at £215,000. It was subsequently increased each year before being slashed to £50,000 in 2011 and then £40,000 in 2014[4]. The number of people reporting pension contributions exceeding their annual allowance soared from 140 in 2006/07 to 41,000 in 2020/21.

The increase in the annual allowance to £60,000 could be particularly beneficial for those whose income means they cross into a higher tax band. For example, someone earning £160,000 a year could make a £60,000 gross pension contribution and see their adjusted net income fall to £100,000. Doing so could enable them to avoid additional-rate income tax and reinstate their tax-free personal allowance (which is tapered once adjusted net income exceeds £100,000).

People on very high incomes could have a lower annual allowance than this because of the annual allowance taper. From 6 April, the tapered annual allowance will kick in once someone has an 'adjusted income' of £260,000 – up from £240,000 currently. The annual allowance will reduce by £1 for every £2 of adjusted income that exceeds this threshold, down to a minimum floor of £10,000 – that's an increase from £4,000 currently.

MPAA lifted to £10,000

In another move that aims to encourage retirees back to work, the money purchase annual allowance (MPAA) will rise from £4,000 to £10,000 from 6 April. The MPAA is triggered when savers flexibly access defined contribution (DC) pensions for the first time, and effectively replaces their standard annual allowance. The MPAA was set at £10,000 when it was introduced in 2015, before being cut to £4,000 from 2017.

Energy bill support extended

To shield households from soaring energy bills, Hunt delayed the planned increase in the energy price cap, which was due to come into force from 1 April. Bills for the average household will remain at around £2,500 per year, instead of rising to £3,000 per year.

Fuel duty has also been frozen and the 5p per litre cut extended for a further 12 months.

Corporation tax hiked to 25%

Despite protests from business leaders, Hunt pressed ahead with a six-percentage point increase in the main rate of corporation tax from 19% to 25%. The increase was first announced by Sunak in his 2021 spring budget, and will come into effect from 6 April as planned.

This will affect businesses with profits of more than £250,000. Companies with profits of £50,000 or less will continue to pay tax at 19% (the 'small profits rate'). Those with profits of between £50,001 and £250,000 will pay tax at 25% but will get marginal relief – i.e., a gradual increase between the small profits rate and the main rate.

Tax breaks for businesses

In an effort to drive business investment and growth, the government will introduce a "full expensing" scheme and reforms to capital allowances, which Hunt claimed would offset the rise in corporation tax. Over the next three years, companies will be able to offset all capital spending against their tax bill in the year it is incurred. This is estimated to save businesses a combined £9bn a year.

Hunt also announced the creation of up to 12 new low-tax investment zones to help "level up" areas outside of London. Each zone will get up to £80m of support over five years, including tax incentives to encourage businesses to those areas.

Other announcements included the provision of £200m for regeneration projects, an additional £200m for local authorities to repair potholes and improve roads (taking the fund to £700m a year), and over £100m of support for local charities and community organisations. There will also be further support for R&D intensive small and medium-sized enterprises via an enhanced rate of tax relief for loss-making companies.

Measures already announced

A whole host of other changes will also come into effect in the new tax year. The key measures affecting investors include:

- The annual capital gains tax (CGT) exemption will be slashed from £12,300 to £6,000. Any profits that exceed the exemption will be taxed at existing rates of 20% for higher and additional-rate taxpayers and 10% for some basic-rate taxpayers (28% or 18% on gains from residential property).
- The annual dividend allowance – the amount of dividend income you do not have to pay tax on – will fall from £2,000 to £1,000.
- The additional-rate income tax threshold (top rate in Scotland) will be lowered from £150,000 to £125,140.
- The personal income tax allowance – the amount you can earn each year before you start paying income tax – will be frozen at £12,570 until 2028, while the higher-rate income tax threshold will be frozen at £50,270.
- The inheritance tax (IHT) nil-rate band and residence nil-rate band will be frozen at £325,000 and £175,000, respectively, until 2028.
- The state pension will increase by 10.1% to around £10,600 a year.

4. https://www.gov.uk/government/statistics/personal-and-stakeholder-pensions-statistics (table 7)

The economy

The spring statement was accompanied by the Office for Budget Responsibility's (OBR) economic and fiscal outlook[5], which painted a somewhat brighter picture for the UK economy than its previous forecast in November. The UK is no longer expected to enter a technical recession this year – defined as two consecutive quarters of declining gross domestic product (GDP). The economy is forecast to contract by just 0.2% this year, a big upgrade from the 1.4% contraction forecast in November. Inflation is expected to fall sharply from 10.7% in the final quarter of 2022 to 2.9% by the end of 2023. Public sector net borrowing in 2022/23 is expected to be £152.4bn, or 6.1% of GDP. This is £24.7bn lower than its November forecast.

However, the OBR warned that the economy still faces "significant structural challenges". Gas prices remain more than twice their pre-pandemic level, business investment has stagnated, the labour force is 520,000 people smaller than expected prior to the pandemic, and productivity has grown at less than half its pre-financial crisis rate. Real household disposable income per person – a measure of real living standards – is expected to fall by a cumulative 5.7% over 2022/23 and 2023/24. While this is 1.4 percentage points less than forecast in November, it would still be the largest two-year fall since records began in 1956/57.

Looking further ahead, the OBR has trimmed its growth forecasts from 2.7% to 2.1% for 2026 and from 2.2% to 1.9% for 2027.

Guy Foster, our Chief Strategist, shares his views on how the announcements could affect the economy and investors.

The context to today's budget was a pretty tense day for financial markets, with Credit Suisse becoming the most significant bank to wilt under investor anxiety. That makes it difficult to note much financial market reaction to a budget which, as usual, had been well leaked in advance.

This had long been billed as a budget to get people back to work. Since 1970, the share of working-age people available for work has risen by about four percentage points, but it peaked when Covid-19 struck the economy. Since the pandemic, there are now 170,000 extra working-age people and 318,000 fewer working-age people looking for work.

The chancellor hopes a combination of carrot and stick measures will reverse that recent decline. The carrot comes from more generous pension arrangements and help with childcare. The stick comes from sanctioning those failing to take up jobs. Age will become a greater headache in the UK as it already is for many other developed economies.

On the other hand, increasing female participation in the workforce has been an extremely effective way of increasing overall workforce participation over several decades. The provision of additional childcare support will hopefully help to mobilise additional labour at a time when the UK is suffering from an acute shortage of workers.

Business investment has been slow over the long term but has improved markedly in recent years. Companies were able to deduct 130% of some of their investment from their taxable profits. That will now fall to 100%. Although the deduction rate is falling, the increase in the rate of corporation tax means the incentive to invest will be strong.

5. https://obr.uk/efo/economic-and-fiscal-outlook-march-2023/

BDM4303 02/23