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Analysis

Is the Labour Win Right for Businesses?

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Biography

Nick Hood is the Senior Business Adviser at the Opus Business Advisory Group (https://www.opusllp.com), the largest independent advisory, restructuring and insolvency firm in the UK.

Nick was a licensed Insolvency Practitioner, working in the business rescue market for 25 years. He is a committed internationalist, having created the largest global network of independent business rescue firms and having also worked overseas in Canada, Milan and Bahrain.

In his earlier career and after qualifying as a Chartered Accountant in 1970, Nick held senior executive positions in major companies in the construction, engineering and media sectors, as well as working for a boutique investment bank.

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Abstract
The UK General Election on 4 July 2024 brought in a new government for the UK, with a very different economic agenda and a wide range of promises to drive UK growth higher. Labour's win has been met with mixed reception from industry commentators and amongst the congratulations there are warnings to the new government 'not to do a Liz Truss and crash the economy'. In this article, the author delves into what a Labour election win means for the business community.

Introduction
The new Labour government has certainly hit the ground running, with the new Chancellor Rachel Reeves leading the charge into the changed economic world so heavily promised during the election campaign. While, it is still very early days, the direction of travel is becoming clear, even if much of the detail is still to be fleshed out. It is inevitable too that some of the initial intentions may need extensive re-modelling once they encounter sustained exposure to the real world of financial market expectations and media scrutiny.

The central focus of the new government's economic policy is a determination to get the sluggish UK economy growing again, both by as much as possible and as quickly as reasonably achievable. Without this, the Chancellor and most pundits agree that the nation's finances will deteriorate even further, with the prospect of even higher taxes or unpalatable spending cuts and possibly both.

It's worth looking first at what is known already about the government's plans, as outlined so far.

What policy initiatives will there be?

There has been an avalanche of announcements in the first few days since the election. Promises made and actions already taken include:

1. Creating a National Wealth Fund.

2. Setting up a range of strategic business policy bodies, including:
   - A Growth Mission Board
   - A Growth Delivery Unit inside the Treasury
   - A Council of Economic Advisers
   - An Industrial Strategy Council

3. Establishing a new entity, Great British Energy to manage the existing dysfunctional energy market.

4. Substantial reform of the Planning system to combat endemic nimbyism and delays to house building and infrastructure projects.

5. Boosting investment in critical infrastructure.

How badly has UK business investment underperformed?

Business investment, which accounts for about 13% of the UK's GDP, has been significantly less than in other developed economies for decades. It has averaged 36% less than other members of the G7 since 1990 according to a report[1] published in 2023 by The International Monetary Fund (IMF).

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Considering the latest disruptions caused by Brexit, the pandemic and the invasion of Ukraine, the IMF also confirms that real-terms business investment in the UK had settled at a slightly lower level by the end of 2022 than in 2016 while other G7 economies experienced a 14% increase on average over this period.

Why does business investment matter?

The link between business investment and GDP growth is an accepted economic fact, though quantifying it is trickier. The previous government's Plan for Growth[2] from 2021 quotes a study, which asserts that a 10% increase in infrastructure capital will cause a 1–2% increase in GDP.

Other research has found that the elasticity of GDP related to the stock of capital in the UK economy is between 0.2 and 0.3, so a 10% increase in the UK's capital stock would raise GDP by 2–3%. With the economy currently still expected by economists to see growth in 2024 of less than 1% and then under 2% in 2025, a serious surge in business investment would be hugely positive for the growth sought by the new government[3].

What is the business world's agenda for economic policy?

A report in 2023 from the independent thinktank, the Institute for Government suggested that government thinking then centred on a stable economy and tax incentives as the conditions that would drive business investment higher[4]. The new government has confirmed that full tax expensing of capital spending will be continued, answering the perceived need for focused tax incentives.

Various surveys have questioned this approach, asking entrepreneurs and other investors what they felt was important. While they welcome tax incentives, most

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downplay their importance, placing them below other factors they rate more highly in influencing a decision to commit to capex. They cite:

- The availability of skilled labour resource.
- The existence of effective local transport and other infrastructure.
- Access to affordable housing.
- Lower interest rates to reduce investment debt servicing costs.

Above all else, what makes businesses invest is an acceptable level of economic and political certainty, or more precisely, the absence of too much uncertainty caused by persistent policy flip-flopping.

The new government's initial announcements address some of these issues, although only a reduction in policy uncertainty and full expensing are short term fixes. Creating the requisite housing, infrastructure and skills will take years to deliver.

What story do the latest signals from the economy tell?

The unexpectedly sharp rise of 0.4% in GDP in May can be seen as an indicator that the economy is firmly on an upward trend[5]. This outcome was twice as high as predicted by economists and followed the disappointing no growth figure for May, but caution is needed in trying to turn a single month's data into a longer-term trend. A better measure will be the outcome for the three months to June as compared to Q1 2024 and the equivalent periods in 2023.

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The fall in CPI inflation to the Bank of England's target rate of 2.0% in May lends further weight to this change of mood, although there are some ongoing worries about the 'stickiness' of some economic statistics, notably core inflation (excluding volatile items such as energy prices) and services sector price increases. The continued high rate of pay growth is another concern.

The one change, which would raise spirits significantly would be a reduction in interest rates by the Bank of England, but the timing and the extent of such cuts remain uncertain. The upsides for both consumers and businesses from reduced debt servicing costs would be considerable.

This is all about business confidence

A positive economic outlook is helpful, as is providing the right incentives for investors and entrepreneurs. Nevertheless, what underlies most decisions to commit to capital projects is simple: it's confidence. This is based on how data and government incentives are interpreted and whether the information makes key stakeholders such as owners, managers and funders not just comfortable, but also enthusiastic about signing off on a potential investment.

The latest Business Confidence Monitor[6] published by the Institute of Chartered Accountants in England and Wales (ICAEW) for Q2 2024 reveals rising confidence. The Monitor is now at its highest level for two years, with businesses expecting input cost inflation to moderate, underpinning further growth in demand and leading in turn to improved profits in the year ahead.

This fieldwork for this report was carried out up to 22 June 2024, so pre-dates the general election and does not consider the initial moves made so far by the new government. It remains to be seen what these developments might do to boost business confidence still further and how soon the confidence shown by the ICAEW Monitor will be translated into real world business investment and ultimately by how much this will impact growth and the strength of the UK economy.

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