



Rt Hon Alistair Darling MP  
Chancellor of the Exchequer  
HM Treasury  
1 Horse Guards Road  
London SW1A 2HQ

17 February 2010

Dear Mr Darling

### **Budget Submission 2010**

Our organisations represent a significant part of the manufacturing industry in the UK. We are writing to you ahead of the forthcoming Budget to outline the steps government should be bringing forward in the coming months to give businesses much needed certainty and confidence as manufacturing and the wider economy return to growth.

### **Outlook for manufacturing**

UK manufacturing emerged from recession in the final months of 2009 following 18 months of extremely difficult trading conditions. Signs of recovery across a broad range of manufacturing sectors in the fourth quarter of last year and indications of continued expansion in activity at the beginning of 2010, offer some encouragement that the sector as a whole will return to growth this year. Nevertheless the global recession has taken its toll, as job losses have been significant across the sector and investment in new machinery has been a particular casualty. EEF's latest Business Trends Survey continues to point to a balance of companies planning to reduce investment over the next 12 months.

Across the economy as a whole an export-led recovery, with manufacturing playing a significant role, looks likely to offer the strongest prospects for growth. But the outlook still remains a fragile and uncertain one. Our central forecast for growth across the economy as a whole is 1.2% this rising, strengthening to 2.2% in 2011. We expect manufacturing output to expand by around 1% in 2010 and 3% in 2011. However, performance within the sector will be uneven. Some parts of manufacturing, particularly those with long lead times on orders, are yet to experience the full extent of the downturn. Business confidence has not yet returned to any great extent, but companies have been preparing for a turnaround in demand. Job losses have been less severe than in previous recessions as companies and employees have worked together to retain skills. In addition, pay restraint has helped companies to maintain competitiveness as they emerge from recession, with unit wage costs beginning to fall back at the end of 2009.

There is a high degree of uncertainty over the path the recovery will take, particularly in the next six months and businesses will, therefore, continue to face a number of risks even as the economy starts growing again. The potential for a high degree of exchange rate volatility is one area that is contributing to a degree of caution, especially for smaller companies as they seek to take advantage of the recovery in the world economy and consider new market potential. And the global economic recovery is still in its infancy and demand could yet falter. There are also continued risks from tighter lending conditions.

However, a significant concern for manufacturers lies around fiscal consolidation and future decisions on taxation and public spending. A number of the stimulus measures that were introduced from the Pre-Budget report 2008 onwards helped to put a floor under the recession and supported demand and access to finance. These measures will come to an end during 2010 or have already done so. While clearly necessary, stimulus measures together with falling tax revenues have left a significant deficit in the public finances.

### **Budget 2010 recommendations**

In our Pre-Budget submission we pressed government to provide stability in the business environment for companies continuing to grapple with an uncertain economic environment. This remains critical for manufacturers. Decisions on investment in workforce development, modern machinery and innovation are all long terms ones, but these decisions will also be key determinants of future competitiveness. Manufacturers, already facing uncertainty about the strength of global markets, face added uncertainty about future business taxes, spending on programmes, such as business support, and government procurement budgets. Any additional spending on new measures in this budget will add to businesses fear about future tax rises, having a negative impact on confidence. In addition, delays in outlining the government's approach to reducing the deficit will keep long term decisions about investment in the UK on hold.

We are mindful of both the economic and political backdrop to the forthcoming Budget and recommend that government take this opportunity to set out the framework departments will use when conducting a forthcoming spending review and future tax changes which will impact on the UK's longer term growth prospects. In particular, UK manufacturers would like clarity on:

#### **1. Timing of deficit reduction**

The Chancellor has already outlined the government's ambition on the pace of deficit reduction. A credible plan for fiscal consolidation and one which allows flexibility should the economic recovery stall is critical. As EEF has highlighted in previous submissions there is a pressing need to restore competitiveness in the UK business tax system, particularly if we want a better balanced economy in the longer term. Laying the foundations of a more predictable and competitive tax system will require the deficit to be addressed swiftly.

Businesses will, therefore, want to see any additional revenues or gains from lower social security spending used to reduce public sector net borrowing rather than diverted into new areas of spending. There should, therefore, be no new spending commitments in this Budget. This is especially critical given that the government is already planning to implement higher rates of corporation tax for small companies and higher rates of employer National Insurance Contributions from April 2011. In addition, rates of business and personal taxation should remain unchanged in this budget.

#### **2. Future taxation**

The need to rebalance the UK economy must remain at the centre of future decisions on taxation and public spending. The UK also needs to develop a modern, efficient tax system that helps to grow a diverse and dynamic manufacturing base. Currently the tax regime is tilted against the productive sectors we need to grow as part of a balanced economy. The proposal to cut Climate Change Levy rebates in the Pre-Budget report was a further example of this.

A modern, competitive tax system should enable small businesses to invest in growth. It should also attract mobile multinational investment to the UK. And provide the predictability needed to minimise the tax risks to those investments. The government must, therefore, think and act more strategically about the role of tax in the economy.

The forthcoming Budget provides an opportunity to outline the foundations of such a system.

- **The UK needs a modern, more efficient tax system.** Over the next parliament, the balance of the tax burden should shift to reinforce the shift to a more balanced economy, one which encourages reinvestment.
- **Create a stable tax environment.** Business will only invest in the UK only if the government calls a halt to the legislative churn, improves the quality of legislation, and allows time for meaningful scrutiny and foster trust in the process. HM Treasury and HMRC should consult with a wider range of businesses.
- **Improve relationships with business.** HMT and HMRC should develop a better understanding of modern manufacturing and adopt a more trusting, risk-based approach to policy and administration, particularly towards SMEs.

### 3. Public spending priorities

The next spending review will impact businesses through decisions on publicly funding support for growth in areas such as training, export promotion and innovation programmes and through the government's public procurement budget. Equally businesses also depend on ongoing investment to ensure reliable transport, communications and energy infrastructure. Across all departmental budgets, savings will need to be found and funding refocused or reprioritised. This will require a critical assessment of both current and capital spending and delivery across all departments. This can only begin with a clear view of what the UK's strategic priorities are in the remainder of this parliament and beyond.

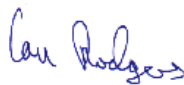
The forthcoming Budget provides an opportunity to signal what these priorities are and the framework within which decisions on future spending plan will be made. This must also include a review of the government's PSA targets in the light of a very different fiscal environment and also in the interests of openness and transparency. There should be no new spending commitments until this process has been completed.

Manufacturers continue to face an uncertain path back to recovery. The Budget must provide the strong signals on the government's economic and strategic priorities that will give businesses the much need confidence to invest for the future.

Yours sincerely



**Martin Temple**  
Chairman, EEF



**Ian Rodgers**  
Director,  
UK Steel



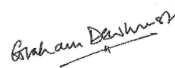
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