

# Prepared for 2 years of political Hokey Cokey? In / Out or shake it all about

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They say a week is a long time in politics. Almost two weeks have passed since the shock election result delivered the first majority Conservative government since 1992. Whilst we now have certainty over the shape of the new Government, and many of its policies, we face even more uncertainty in other areas. The next two years could be a very long and defining period in politics from an EU, UK and Northern Ireland-perspective.

The failure to elect a Labour led government means their planned increase in the corporation tax rate (*to 21% initially*), the introduction of a mansion tax on homes worth £2m+ and the reintroduction of a 50p income tax rate will not happen. In addition, the 'bedroom tax' will not be abolished.

Meanwhile George Osborne will get his first opportunity to deliver a 'Blue Budget' on the 8<sup>th</sup> July and the first Conservative Budget since November 1996. This will be a vehicle for delivering the Conservatives' manifesto pledges.

On the tax side, barring U-turns, this means there will be no rise on rates of VAT, national insurance contributions and income tax. A coalition government would likely have seen these generous pledges watered down. In light of these ring-fenced tax freezes, one can expect a smattering of stealth taxes to be introduced sooner rather than later.

There is a strong incentive for the government to frontload the fiscal pain in the first two years of this Parliament so as to ease-off in time for the 2020 General Election. The recent election effectively acted as a speed camera on the pace of austerity. Now that this has passed, the Chancellor is expected to put his foot down on the austerity accelerator.

On the spending side, the cuts in Departmental spending over the next two years are expected to be more severe than any of the cuts delivered in any year over the last five.

We will get more clarity on the UK spending cuts in this autumn's Spending Review (SR). This will set public spending totals for the next 3-4 years. In turn, SR 2015 will determine Northern Ireland's spending allocations via the Barnett Formula (*which may be reviewed in this Parliament to the detriment of Northern Ireland*).

Welfare spending is also set to be cut by an additional £12bn as flagged before the General Election. This will include a 2-year freeze on working age benefits from April 2016 and a lowering of the annual benefits cap from £26,000 to £23,000. Further detail surrounding these cuts will emerge in the coming weeks.

Given the dire state of the UK public finances it would be desirable to have no major political distractions to deflect the government from addressing this priority. Unfortunately this will not happen.

The return of a Tory government with an outright majority and enhanced mandate means an 'In-Out' EU referendum will be delivered by the self-imposed deadline of 2017. However, from a business and political perspective the sooner the period of uncertainty ends the better.

Last week the UK's Foreign Secretary, Philip Hammond, gave his most enthusiastic backing for the UK's place in a reformed EU as opposed to Britain exiting the EU. The latter is dubbed 'Brexit' which follows the term 'Grexit' given to the potential for Greece to leave the Eurozone. Mr Hammond aims to support the "Yes" campaign for remaining in the EU and wants a deal as fast as possible without insisting on an EU treaty change. This raises the prospect of a referendum occurring in 2016 ahead of elections in France and Germany in 2017. However, without Treaty change this is likely to involve a limited set of concessions ahead of a referendum vote. These would likely include: guarantees for the City of London against discrimination by the euro area; dealing with the problems of 'welfare tourism' and vetoes on any moves to further EU integration.

Last year UK politics was dominated by debating the pros and cons of the Scottish referendum on independence, or 'Scexit'. The next two years will focus on the merits or costs of the UK remaining in the EU or leaving it (Brexit).

Given the success of the Scottish National Party (SNP) in the latest General Election, the Scexit issue has not gone away. We can expect Westminster to provide Scotland with additional fiscal powers and greater fiscal autonomy. This could trigger a fiscal powers arms race within the UK's cities and regions. England is now joining in on the devolution party. Westminster has already sought to devolve greater fiscal powers to areas of England including the development of the so called 'Northern Powerhouse'. Last week James Wharton was appointed minister for the Northern Powerhouse.

2017 remains a key date for Northern Ireland too as corporation tax setting powers will be devolved by then. However, this is dependent upon delivering on a number of interlocking agreements which formed the Stormont House Agreement. Delivering welfare reforms that have been adopted in the rest of Great Britain, including by the anti-austerity SNP in Scotland, are central to this.

Reform of the EU is seen as essential. However, Welfare Reform (WR) in Northern Ireland is controversial with the Stormont Executive's failing to agree a way forward. Opting out of the UK Welfare Reforms (WR) or 'Wrexit' is creating financial pressures that the Northern Ireland Executive's budget cannot absorb. Already, this has led to the build up of a financial black hole of around £500m which could necessitate Northern Ireland to announce its first Emergency Budget at next month's Monitoring Round.

It could be said that the next two years are set to be characterised by the lyrics of a well-known 1940s dance hall song. When it comes to the UK's relationship with the EU, the left want in, the right want out, and some on the right of the middle want to shake it all about (i.e. reform). And there's plenty of in / out deliberation to be done at a UK domestic and NI political level too, with the question of Scexit and even Stexit – where some have speculated that the welfare reform impasse (Wrexit) could lead to the reintroduction of direct rule. So we're set for Hokey Cokey politics. Uncertainty is what it's all about.

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