



The emergency budget has been and gone and whilst much of the content was anticipated, our direction is now clearer.

The markets also seem content that a combination of higher taxes and lower public spending is in the countries' best interest.

Its payback time

In a controversial "emergency" Budget aimed at reducing the UK's spiralling debts, Chancellor of the Exchequer George Osborne announced sweeping - and contentious - cuts in spending on benefits and public services, accompanied by higher taxes.

VAT is set to rise from 17.5% to 20% from 4 January 2011, and the increase is expected to raise £13bn of additional revenue by the end of 2011. Capital gains tax has risen from 18% to 28% for higher-rate taxpayers. However, the personal income tax allowance will increase in April 2011 by £1,000 to £7,475, removing 880,000 people from the income tax system.

The Chancellor instigated average real budget cuts of 25% to most government departments over four years. Elsewhere, changes to the welfare system are expected to save £11bn by 2014/15. From 2011, tax credits, benefits and public service pensions will increase in line with the Consumer Price Index rather than the Retail Prices Index, which tends to be higher. Child benefit will be frozen for three years and tax credits cut for families earning more than £40,000. Housing benefit will be capped at a maximum of £400 per week. Meanwhile, from April 2011, the basic state pension will rise in line with earnings, prices or 2.5% - whichever is the largest.

The threshold at which employers begin to pay National Insurance will rise from April 2011 by the rate of inflation plus £21 per week. Meanwhile, corporation tax will be reduced in 2011 to 27%, and then by 1% every year until it reaches 24%. Turning to the financial sector, the Government is set to introduce a bank levy that it expects to raise £2bn per year. It will apply to UK banks, building societies and the UK operations of overseas banks, but will not apply to smaller banks.

Reaction to the Budget was mixed, with the Confederation of British Industry hailing it as "the UK's first important step on the long journey back to economic health". However, opponents protested that the Chancellor's measures risked triggering a "double-dip" recession.

For its part, the Institute for Fiscal Studies described the Budget as "a mixed bunch of positive reforms, backward steps and missed opportunities." Looking ahead, the UK economy is forecast to expand by 1.2% in 2010, 2.3% in 2011 and 2.8% in 2012. Debt is expected to peak at 70% of GDP in 2013/14, while the budget deficit is forecast to be in balance by 2015/16.

Surviving recession

TIP No 2: CONSIDER LOOKING OVERSEAS

With diversity in mind, perhaps you can start looking overseas for opportunities. A UK focused portfolio is a sensible and conservative option for a UK based investor. However, this strategy leaves you at the mercy of only domestic sentiment. Other areas of the world might offer a more positive outlook during this time, or could simply be better placed to help through a domestic downturn.

You need to be aware of the additional risks involved with international markets but even a first step into developed, western economies could diversify some risk.

Inflationary pressures rise

UK interest rates have now remained at their all-time low of 0.5% for over a year. The UK has crept tentatively out of recession but the new Government are now anxiously looking at ways to cut costs without doing anything to derail a very fragile recovery.

However, the UK Consumer Price Index reached 3.4% during March. In his open letter to the Chancellor of the Exchequer back in January, the Governor of the Bank of England (BoE), Mervyn King considered the rise to be a "temporary deviation" and suggested inflation will fall back below the Government-set target level of 2% in the second half of 2010. Even taking King's explanation for the sudden rise in prices into consideration, it is worth remembering the rate of inflation has almost doubled since November 2009. Indeed, only a few months ago, deflation seemed the more credible risk. In normal circumstances, the BoE would increase the cost of borrowing in order to cool inflation. However, rates are unlikely to rise in the short term because policymakers fear higher interest rates could endanger the UK's economic recovery.

Low interest rates are generally good news for borrowers, but are bad news for savers, who have already endured a year of exceptionally low interest rates. Returns on cash are meagre and high inflation is eroding the real value of cash. Looking ahead, Britons face the combined problems of high inflation and rising taxes, both of which will put additional - and unwelcome - pressure on disposable income.



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