UK Budget: Will asking business to invest pay off?

- **The tax changes, the expectation and the reality, and what the impacts might be on private markets**
- **What the Chancellor promised and how business will hold her to those promises**
- **The numbers that could aid fundraising and deal making in sectors earmarked for growth**

Chancellor Rachel Reeves' inaugural Autumn Budget delivered expected tax rises, as well as clarifying the government's position on growth areas in what was termed a 'modern industrial strategy'. ***Matt Horton*** *dissects the Autumn Budget for private fund managers.*

In the run up to the Budget there was a lot of speculation about how carried interest would be taxed. In the end though the rise on carried interest was 4%, from 28% to 32% effective from April 2025. Though Reeves did also say there'd be further reform in the next Budget, it does keep the rate competitive with other jurisdictions and is unlikely to have the chilling effect a rise to 45% would have had if carried interest were treated as income instead of as capital gains. Broadly, the change has been cautiously welcomed by private markets.

"We recognise that the Government has had to balance the need to raise revenue for essential public services with the requirement to keep our economy competitive," the British Venture Capital Association (BVCA) said of the Budget.

"The announcement on carried interest recognises that a tax treatment which reflects the long term, risk-based nature of private capital investments is necessary to ensure that this important UK sector can continue to flourish in an increasingly competitive international environment."

Overall, the capital gains tax rates were increased from 10% to 18% for the lower rate, while the higher rate rises from 20% to 24%. In addition, the government has extended the freeze on the threshold for inheritance tax.

The removal of the non-domicile rule could have implications for private markets managers, however the government's reasoning is that if you make the UK your home, you should pay tax in the UK. For private markets this might mean retaining talent in the UK will be more difficult as they seek more tax friendly domiciles. The new residence-based system means that new arrivals to the UK will be exempt from tax on their foreign income and gains for their first four years living in the UK.

Answers to three questions fund managers are asking following the Budget:

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Business asked to pay for public service investment

It is a tax-heavy budget for business with the tax increases earmarked to invest significantly in public services. Employers National Insurance contributions for each employee will rise, as will the minimum wage. Corporation tax, though, will not. An area of concern for start-up businesses is the expected changes to the Business Asset Disposal Relief (BADR). At present, when founders sell their businesses, BADR sets tax at 10% on exit takings, up to a threshold of £1m. This rate remains this year but will rise to 14% in April 2025 and 18% thereafter.

Though the growth forecasts given by the Office of Budget Responsibility (OBR) were lukewarm for the next five years, there is the possibility that the focus on strengthening tech and innovation sectors will provide opportunities for growth, especially for investors looking for stability.

That was the overriding message of Chancellor Rachel Reeves' budget – a return to stability. For business, across the board, this will be a welcome message even if the cost of that stability is seen to be coming out of business' pocket.

Stability will likely better support fundraising and dealmaking. Though the tax rises could impact talent retention and job creation, they do not make the UK uncompetitive among its G7 peers in terms of corporation tax rates. The G7, which is comprised of the seven wealthiest nations in the world, has an average statutory corporate income tax rate of 26.77% and a weighted average rate of 26.24%. The Organization for Economic Co-operation and Development (OECD) member states have an average statutory corporate tax rate of 23.57% and a rate of 25.83% when weighted by GDP.

The promise business will hold Reeves to is her rationale for the budget, laid out in this quote.

"First, and most important, is to restore economic stability. That is my focus today.

"Second, increasing investment and building new infrastructure is vital for productivity, so we are catalysing £70bn of investment through our National Wealth Fund and we are transforming our planning rules to get Britain building again.

"Third, to ensure that all parts of the UK can realise their potential, we are working with the devolved governments and partnering with our Mayors to develop local growth plans.

"Fourth, to improve employment prospects and skills we are creating Skills England, delivering our plans to Make Work Pay and tackling economic inactivity.

"Fifth, we are launching our long-term modern industrial strategy and expanding opportunities for our small and medium sized businesses to grow.

"Sixth, to drive innovation we are protecting record funding for research and development to harness the full potential of the UK's science base.

"And finally, to maximise the growth benefits of our clean energy mission, we have confirmed key investments such as Carbon Capture and Storage to create jobs in our industrial heartlands."

The budget in numbers:

£5 billion – government investment to deliver 1.5 million homes

11 – the number of new green hydrogen projects.

£1 billion – budget earmarked for investment in the aerospace sector

£2 billion – for the automotive sector, with a focus on supporting electric vehicle production

£70 billion – the amount of private sector investment the National Wealth Fund will mobilise

£20 billion – for research funding across areas such as engineering, biotechnology and medical science

£520 million – to find a new Life Sciences Innovative Manufacturing Fund

The business community, and private markets in particular, will be hoping that the stability promised in the budget will mitigate the additional cost of doing business that the increased taxes will bring. The Institute of Directors summed it up in their reaction statement: "Business leaders can only hope that this is a big bang now, to wipe the slate clean, and that there will be no further shocks of this magnitude in the lifetime of this Parliament, enabling business to plan with more confidence."

If you'd like to discuss any of the statements made in the budget roundup, please contact Matt directly.