Extract from briefing provided to First Minister, updated 28 July 2020

<u>As well as investing in supporting the economy we are also developing policy to support our recovery</u>

- On 29 June we published *COVID-19: UK Fiscal Path – A New Approach,* in which we called for the UK Government to take a number of actions, including:
    - A UK-wide £80 billion stimulus package to deliver an investment-led recovery, accelerate the transition to net zero and build an economy that has the broader wellbeing of the population at its heart.
    - A temporary reduction in VAT, as one of the quickest ways to provide an additional spending boost to support the sectors of retail, hospitality, leisure and tourism that have been most impacted by the lockdown.
    - A National Debt Plan to avoid a return to the austerity of the past by adopting flexible fiscal rules.
    - A jobs guarantee scheme for young people, recognising that the pandemic has a disproportionate impact on young people, who tend to work in sectors hardest hit by coronavirus, while graduates will find it harder to find a job in a recession.
    - A renewed call for the UK Government to extend the Brexit transition period to avoid a second economic shock following that caused by the pandemic.

Extract of briefing provided to Cabinet Secretary for Finance, updated 1st July 2020

ISSUE – The UK Chancellor is expected to set out further fiscal stimulus measures in his summer statement on 8 July. He is reportedly considering a temporary reduction in VAT, including for the Hospitality sector, immediate funding for capital spending projects and support for the under 25s. Some press reports indicate that this could be followed by a tax raising budget in the Autumn.

ISSUE - 30 June: The Prime Minister announced that he will bring forward £5 billion of capital investment projects under a review of planning rules, dubbed Project Speed, in order to aid the economic recovery. However, there is no "new" funding, or extra Barnett consequentials for Scotland as all funding is recycled from existing budget plans announced at March 2020 Budget. He refused to rule out the possibility of tax rises.

ISSUE – 29 June: The Scottish Government publishes a paper calling upon the UK Government to deliver a further fiscal stimulus of 4% of GDP (£80 billion) to kick-start the economic recovery. The paper sets out ten principles the UK Government should follow to manage the economy and public finances through the recovery.

ISSUE – 29 June: The STUC has backed the SG's calls for a UK fiscal stimulus focused on job creation - through public works, investment in clean infrastructure projects and investment in education and social care. The STUC supports an extension of the furlough scheme for the hardest-hit sectors alongside a Jobs Guarantee. However, unlike the SG, the STUC opposes VAT cuts arguing that this disproportionately benefits the better off.

ISSUE – 26 June: Although VAT cuts have been successful in stimulating demand in the past, the Institute for Fiscal Studies (IFS) argues that the case for such a tax cut is currently mixed and the Government may be better to adopt a wait and see approach. (IFS, June 26)

We have set out bold and practical proposals for a UK-wide £80 billion (4% of GDP) fiscal stimulus to regenerate the economy and reduce inequalities.

- Our proposal recommends bold, practical steps which would provide an immediate boost to our economy, protecting existing jobs and delivering new ones. It tackles public sector debt, employment and proposes measures to further support business.
- Germany has already adopted a similar-size stimulus package, representing 4% of GDP, and the UK needs to be similarly positive and proactive.
- The UK Government should take advantage of historically low interest rates and invest in further capital spending to deliver an investment led recovery.
- The International Monetary Fund have found that temporary, targeted, and well timed government stimulus packages can lead an economic recovery.
- Accelerating the transition to a net-zero economy through major investment in low carbon as well as digital infrastructure should be at the heart of any stimulus package.
- The package must also include further Barnett consequentials to enable us to invest in our economy and shape our own response to the pandemic.
- Underpinning our approach is a belief that economic stimulus and tackling inequality must be prioritised over deficit reduction until the economy recovers.

- Action is needed now – but if the UK Government is not prepared to take that action then Scotland must have the additional financial powers which are essential to secure a sustainable economic recovery. Without those powers we would be left at a severe disadvantage to other nations, and would effectively be trying to chart our way to recovery with one hand tied behind our back.

There must be no return to the fiscal austerity of the past.

- Our number one priority is to ensure no return to the damaging austerity of the past – such a response would damage our economic and social recovery from COVID-19.
- The UK Government should not return to the ideologically-driven austerity agenda which characterised the period following the financial crisis.
- Today we know that this has not only undermined economic growth and reduced valuable resources, including for the NHS, it has also had a disproportionate impact on the most vulnerable individuals in society.
- As we face the biggest economic crisis in our lifetime, growing the economy and tackling inequality must take priority over deficit reduction until the economy recovers.
- Fiscal rules should not constrain the fiscal policy response, thereby weakening the economic recovery and doing more harm to the long term fiscal position.
- The crisis will inevitably lead to an increase in public debt, with latest public finance figures suggesting that debt, as a share of income, exceeds 100% for the first time since the 1960s.
- This debt will need to be managed down over a long period and in ways that aid, rather than hinder, economic recovery.
- A number of think tanks and economic commentators share our view that fiscal sustainability should be measured in terms of public sector net worth: *"The pandemic presents a unique opportunity for governments to consolidate their finances by looking not just at spending and revenues, but also at assets and liabilities. By taking an integrated approach, as would be done in a corporate restructuring, governments can steer their way toward a stronger recovery without the need for excessive austerity and the social hardship that comes with it."* (Willem Buiter, Columbia University, 26 June).

The Chancellor must cut VAT for Scotland's crucial Tourism and Hospitality sector to 5% and reduce the standard rate of VAT to stimulate consumption.

- We are taking action to support employers and employees impacted by COVID-19. This includes 100% rates relief for retail, hospitality and leisure properties, rates relief for all non-domestic properties across Scotland, and a £185m fund to support newly self-employed people and affected SME businesses.
- However, our powers are limited. The Chancellor must go further to support the restart and recovery of Scotland's hospitality industry by cutting VAT, particularly for hospitality.
- This should be a temporary package, until the economic recovery has begun, and timed to coincide with the lifting of restrictions on the hospitality industry across all parts of the UK.
- An ill-timed fiscal stimulus would risk wasting valuable resources and having less of a positive economic impact if consumers cannot make use of tax incentives as shops, pubs and restaurants remain closed.

- A temporary package would encourage consumers to spend as and when businesses re-open rather than delaying purchases until the economic outlook is less uncertain.
- There is evidence that cutting VAT has been effective at stimulating consumer demand in the past. For example after the Financial Crisis a temporary VAT cut succeeded in boosting consumer sentiment and retail sales (IFS, June 26).
- The stimulus package should finance a temporary reduction in VAT to 15% and move the tourism and hospitality industries onto a reduced VAT rate of 5%.

The Chancellor must take decisive action to help firms create jobs, support young people into the labour market and reduce inequalities.

- COVID-19 and necessary physical distancing measures are having a major impact on Scotland's labour market. Economic activity has fallen, businesses have closed and firms have paused recruitment.
- The Scottish Government has been working tirelessly to keep businesses afloat and ensure as few people as possible lose their jobs. So far this has included a tailored package of more than £2.3 billion in business support.
- However, employment law, which includes setting of the legal minimum wage, is reserved to the UK Government as is National Insurance.
- The stimulus package should finance a two pence cut in employers' National Insurance Contributions to reduce the cost to businesses of hiring staff.
- Scottish Government analysis shows the shutdown will hit younger workers the hardest as employees aged under 25 are more likely to work in a sector that is now shut down as other employees. Women are also more likely to work in a sector that has shut down than men.
- To prevent mass redundancies and long term joblessness, the UK Government should provide a jobs guarantee scheme for young people and extend sector specific employment and business support schemes.

Annex A: Summary of the Ten Principles

Public Finances

1. Avoid a return to the austerity of the past and adopt flexible fiscal rules. Growing the economy and reducing inequality should take priority over deficit reduction until the economy has fully recovered.
2. Introduce a fiscal stimulus package worth £80 billion, or 4% of UK GDP, to deliver an investment-led recovery, accelerate the transition to net zero and build an economy which has the broader wellbeing of the population at its heart.
3. Cut the standard rate of VAT to 15% for six months once current restrictions have been lifted across the UK. Reduce VAT for the hospitality sector to 5%.
4. Accelerate major investment in low-carbon, energy efficiency and digital infrastructure and recognise the value of this investment by assessing the government's fiscal sustainability in terms of its public sector net worth.
5. Enable Scotland to shape its own response to the pandemic by providing further consequentials for investment into the Scottish economy and by extending Scotland's fiscal flexibilities.

Support the labour market and improve the welfare safety net

6. Choose to use public money to protect jobs and livelihoods through support schemes and increase the responsiveness, accessibility, generosity of the UK welfare safety net, so that it provides sufficient support for people in and out of work.
7. Introduce a jobs guarantee scheme for young people, increase training, and continue sector-specific employment and business support schemes where needed.
8. Create jobs through a significant reduction in firms' labour costs by cutting employers' National Insurance Contributions and removing the costs of the apprenticeship levy.

Dealing with debt

9. Agree a national debt plan to support businesses, households and the banking system through the economic recovery and manage debt recovery over a longer time period.
10. Reset the monetary policy objective of the Bank of England so that long-term growth and reducing inequality are promoted.