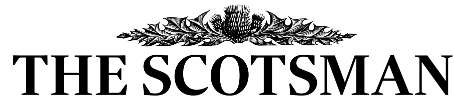

THE SCOTSMAN

Why lower VAT won't cut it on high street of queues and masks

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June 21, 2020

But woe, it seems, for Scotland. Last week respected senior SNP figure Andrew Wilson made a dire prediction on BBC Scotland that Scotland would have the worst performing economy in the developed world.

"What's clear to me," he said, " is the UK is set to be the worst performing economy in the developed world and Scotland's probably going to be a bit worse because of the nature of our sectors and how the virus has behaved north and south of the border.

"I think this is a long haul back, not a V-shaped bounce back at all… We need a monumental effort – politicians and governments working in collaboration – to get the measures we need in place to rescue businesses. Because the outlook for people, for families, is bleak."

Oh, dear. Time was when SNP spokespeople lost no time in highlighting those occasions when the economy in Scotland showed some infinitesimal gain in economic performance relative to the rest of the UK. Now it is tasked to explain why the opposite is true.

Scotland's GDP fell by 2.5 per cent in the first three months of this year – a period that only covers a few weeks of lockdown. And new statistics also estimate that economic activity north of the border slumped by 18.9 per cent last month. It means the economy is likely to have dipped by nearly a quarter in the first six weeks of lockdown.

Comparable figures for the UK show the economy shrank by two per cent over the same period.

As for retail sales in Scotland, these plunged by 27.6 per cent in May compared with May 2019 – the second lowest recorded by this monitor since its inception in January 1999.

In contrast, UK retail sales recorded a small recovery, with the amount of goods sold rising by 12 per cent after record falls in April. Sales were boosted by a 42 per cent rise at household goods stores, with DIY shops and garden centres reopening. "Non-essential" retailers in England and Northern Ireland have also since been allowed to reopen. But most shops in Scotland will not re-open until 29 June.

As for the economy overall, the MPC pointed last week to latest indicators suggesting that UK economic activity had started to recover in May after GDP fell 20.4 per cent month-on-month in April, and that the quarter-on-quarter fall in GDP in the second quarter was likely to be less than it had expected in its May Monetary Policy Report.

Three factors may help account for this variance north and south of the border. First, North Sea oil and related onshore activity has been badly hit by the slump in the oil price and notably weaker global demand.

Second, our tourism and hospitality sectors account for a greater share of economic activity and employment relative to the rest of the UK. So, the shutdown of hotels, restaurants, pubs and B&Bs are hitting us all the harder.

And third, the Scottish Government has been more cautious in relaxing the lockdown measures, with many high street shops still shuttered while partial re-opening was allowed south of the border.

The UK government has been under increasing pressure from the business sector to relax lockdown measures and to ease the social distancing rules from the current two metres.

But here the business sector appears to have struggled to gain the same urgency of attention from First Minister Nicola Sturgeon and the Scottish cabinet. The priority has been to check the spread of the deadly Covid-19, particularly in hospitals and care homes. Against this, the economic consequences of prolonged lockdown do not seem as yet to have weighed so heavily. However, this may change as the full force of lay-offs and redundancies across the economy start to be felt.

Meanwhile, the relatively better performance of the retail sector in the rest of the UK has certainly triggered no surge in optimism. Samuel Tombs, chief UK economist at Pantheon Macroeconomics, cautioned that the "overall consumer picture remains bleak… May's recovery in retail sales," he said, " should not be interpreted as a sign that the economy is embarking on a healthy V-shaped recovery from Covid-19.

"Retail sales account for only a third of households' overall spending. Naturally, spending on goods will recover faster than on services, which usually require human contact and remain largely unavailable."

A temporary reduction in the rate of VAT from 20 per cent to 15 per cent has been mooted as a means to boost consumer spending and lift high street demand. Such a cut was deployed by prime minister Gordon Brown in 2008, when the rate was lowered from 17.5 per cent to 15 per cent in the wake of the financial crisis.

The IMF has suggested repeating the move. And John Hawksworth, PWC UK's chief economist, says a cut now would help bring people back on to the high street.

Chancellor Rishi Sunak reportedly wants such a cut. But would it really work to boost consumer confidence and lift retail purchases? Would a reduction of some three per cent on pricey durables such as household goods and gadgets really tempt apprehensive savers to overcome their fear of the virus?

Cato Institute economist Ryan Bourne disagrees. A VAT cut, he wrote last week, "would be a worrying misdiagnosis of our current travails". The biggest uplift to sales is more likely to come, not just from a re-opening of high street shops but also from a return of some normalcy in the store environment. Long queues, face masks and social distancing militate against a full throttle return to normal.

"Sunak's proposal," says Bourne, " is premised on the idea that consumers won't spend. But it's much more likely that their savings are, and will remain, elevated. While we can expect a sharp bounce back in certain spending areas as lockdown regulations are eased, the sad truth is we will see ongoing disruption on the supply and demand side of the economy because of the virus. It is that, not consumer irrationality or lack of money that will prevent a full V-shaped recovery."

We have it seems, to be patient awhile yet.