SPRING FISCAL STATEMENT

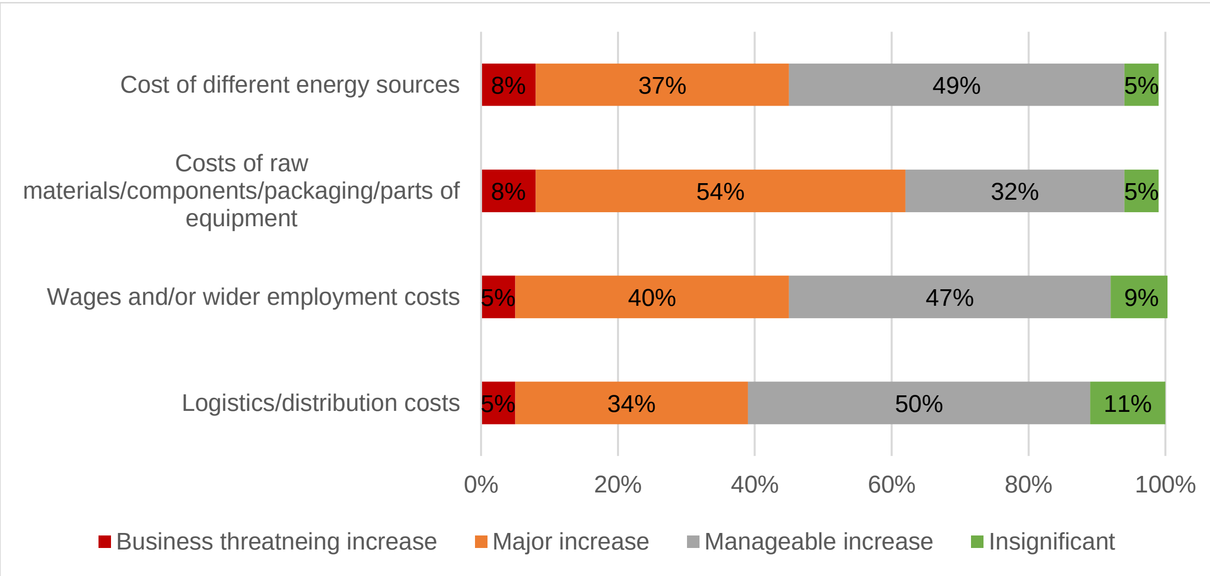
Make UK's submission to HM Treasury Spring Fiscal Statement

Introduction

1. Sustained, stable growth remains the shared goal of industry and Government for 2022. Following two years of economic suppression, it's now, in this so-called recovery period, that UK manufacturers are eager to make the most of their swelling order books to recoup as much of the lost value as possible. As such, the Spring Fiscal Statement comes at a critical time for manufacturing in the UK. The sector finds itself in a juxtaposition between soaring domestic and international demand for British manufactured goods and extreme supply-side limitations that are seeing manufacturers struggle to maintain production capacity.

2. At this Spring Statement the Chancellor must not shy away from the realities facing manufacturers today. They face a multitude of increasing cost pressures from the soaring cost of raw materials, snowballing wage inflation, to spiralling energy costs - all of which could prove to be existential threats to the industry. All the evidence points to a situation where an increasing number of manufacturers face a fight for survival, in fact, almost 1 in 10 businesses see the rising cost of raw materials and energy as business threatening[1].

Chart 1: Hierarchy of severity of cost increases to manufacturers



Source: Make UK, Manufacturing Monitor, February 2022

3. Our Manufacturing Outlook for Q1 in 2022 shows UK manufacturing experienced a slow-down in output and orders indicating the pandemic's rubber band effect is fading. Despite the key indicators showing the sector continues to grow, the sector is losing momentum – and fast. Margins have effectively collapsed as

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[1] Make UK, Manufacturing Monitor, February 2022

inflationary pressures reach new heights. Prices for UK goods have expanded at the fastest rate yet, reporting a balance of 58%, with export prices reporting a balance of 50%. These continue to be some of the highest balances in Make UK's survey history and the trend suggests higher prices are set to become locked in[2].

4. Furthermore, the evidence shows that these price rises are now being passed on. The latest balances show a large share of manufactures are reporting declining margins, with a balance of -21% of manufacturers reporting worse UK margins. Similarly, a balance of -13% reported the same for export margins. While manufacturers are clearly raising their factory gate prices, in other words, the prices of their finished goods, at an alarming rate, it is still proving to be insufficient to offset the erosion to their operating margins.

Chart 2: Key manufacturing indictors for Q1 2022

Indicator	Balance	Change	
Confidence	7.1	↓	Business confidence remains high but falls again
Output	24%	↓	Output balance growth slows further
UK orders	30%	↓	UK orders growth slows further but maintains dominance over exports
Export orders	18%	↓	Export orders growth slows further
Employment	26%	↑	Jobs improves on balance
Investment	27%	↑	Investment intensions recover following slowdown

Source: Make UK, Q1 Manufacturing Outlook, March 2022

5. The consequence of all this is that business confidence is falling, and with little sign of respite on the horizon, failure to address the spiralling cost of doing business right now, will risk these short-term challenges becoming baked in. Crucially, it risks our long-term ambitions to transition to a net zero economy and build resilient workforces, becoming a distant reality. As a result, we are urging the Chancellor to use this Spring Fiscal Statement to address these immediate threats head-on, to give us the best chance of mitigating the catastrophic impacts manufacturers face.

Summary of key measures to take

6. The key measures we are urging the Chancellor to take this Spring Fiscal Statement are:

- Delay the planned National Insurance Contribution rise in April until the economy is in a more robust position.
- Reinstate business rates relief for small businesses and bring forward the improvement relief and investment relief exemptions by 12 months.
- Tackle spiralling electricity costs by reducing the policy costs, in conjunction with:
  - Reducing the carbon price via the cost control mechanism within the UK ETS providing immediate support for all manufacturers.
  - Removing the additional Carbon Price Support (CPS) tax that only UK consumers pay, which would drive down the electricity price.
  - Considering removing the Climate Change Levy entirely to further reduce costs.
  - Increase the relief from the Renewables Levies now that the UK is no longer subject to EU State Aid rules
  - Increasing compensation for the indirect cost of carbon, benefitting the most trade-exposed and energy-intensive industries
  - Implementing network cost reductions for the most electro-intensive industries
- Increase and extend the Industrial Energy Transformation Fund.

[2] Make UK, Q1 Manufacturing Outlook, March 2022

- Reintroduce trade credit reinsurance as well as liability holidays for those companies straddled with debt.
- Extend the Super Deduction scheme with a view to making it permanent at the Autumn Budget.
- Introduce an Employer Training Fund to support businesses and workers to reskill and upskill.
- Instruct the Migration Advisory Committee to review the shortage occupation list and introduce an emergency temporary visa route
- Announce a further extension for CE marked products to be sold on the UK market for products where the legislation in the UK remains the same as in the EU.
- Extend the Export Support Service remit to support businesses in the importing of goods to the UK.

Limiting the tax burden

Delay the planned National Insurance Contribution rise in April until the economy is in a more robust position.

7. The planned National Insurance Contributions (NICs) hike comes at an astoundingly inopportune time for UK manufacturing, not least because it will add to what are already soaring costs for UK businesses, but it will directly work against manufacturers' efforts to secure labour in the industry during an unprecedented shortage of workers. In fact, 60% of manufacturers say the National Insurance rise will have a moderate or significant impact on recruitment[3].

8. The planned NICs rise stands to be an anchor on the consumer economy, in particular it will further worsen one of the most significant challenges manufacturers are facing in their business at the moment: the shortage of labour. It's this inability to fill roles reliably that is leading to the industry's inability to fulfil their booming order books, in turn leaving individual manufacturers 'missing out' on maximising their potential during the post-pandemic recovery period.

9. The planned NICs rise should be postponed until the economy is in a more robust position, a position where such a significant change such as this wouldn't stand to threaten what is an already fragile economic recovery. We believe that the public purse should be recouped not through means of taxing the supply-side during a supply crisis, and instead, should focus on means of recovering the purse through growth.

10. Further to the potential damage to the manufacturing sector's recovery, the inflationary implications to the wider economy are significant. While input inflation is soaring, consumer inflation is rising at a concerning pace too. If this NICs rise comes to pass, the majority of manufacturers indicate that they are likely to pass this cost directly onto customers, further fuelling the inflationary fire that will continue to trickle down into the consumer economy.

Reinstate business rates relief for small businesses and bring forward the improvement relief and investment relief exemptions by 12 months

11. Manufacturers face catastrophically high-cost increases that endanger their operational viability to similar levels experienced during the height of the pandemic. For this reason, especially for small businesses, the Government must reinstate the 12-month business rates relief mechanism that was utilised during the COVID-19 pandemic. This will ease the cost pressures manufacturers are facing as many businesses are already considering shutting down temporarily to reduce energy consumption. For businesses that may not qualify for this relief, the Government should bring forward the improvement relief exemption from 2023 to 2022 so that they can better manage their cashflow whilst still plan productive property investments.

12. As the energy crisis spirals out of control, and the recent conflict between Russia and Ukraine promising to worsen the situation, manufacturers should be correctly incentivised to invest in self generation of energy and storage. The Chancellor announced the investment relief to business rates that will exempt green property investments from rate reviews but plans to bring this in from 2023. As the UK announced its plans to reduce its consumption of Russian fuels by the end of this year it is imperative that businesses are not penalised for investing in green property improvements. Therefore, the Government should release this exemption as soon as possible by bringing it forward from 2023 to 2022.

[3] Make UK, Manufacturing Monitor, February 2022

Reducing soaring business costs

Tackle spiralling electricity costs by reducing policy costs and increasing and extending the Industrial Energy Transformation Fund.

13. Already operating in the context of historically high electricity costs, the recent gas commodity crisis has sent energy prices spiralling. Electricity wholesale and gas prices have increased between 8-10 times compared to a year ago. Some manufacturers that have recently renewed tariffs have found themselves facing significant price rises. These significant price hikes will also hit the big energy users who have been operating a hedging policy rather than contracting with suppliers at an agreed price. Energy bills are predicted to increase up to 5-fold in some cases from today's prices. These prices are predicted to stay at those levels through the whole of 2022 and the winter of 2023-2024.

UK household energy efficiency comparison

UK households and manufacturers are faced with an unprecedented energy price spike. While it's vital that Government ensures a clean, secure, energy supply – the cheapest, cleanest energy is energy we don't use.

Domestic energy use is the second highest area of consumption in the UK and its usage has remained static at roughly the equivalent of 40 million tonnes of oil per annum for nearly 50 years. In addition, the built environment accounts for 40% of UK carbon emissions in the UK and 60% of all waste.

In Scandinavia and Japan, high energy performance standards in domestic buildings free up Government capital to support crucial energy intensive industries while ensuring bills remain affordable to consumers.

Government should introduce robust minimum energy performance standards for all new homes by committing all new build housing stock to perform at EPC A by 2025. This would safeguard homeowners against rising costs, alongside reducing energy demand, and wholesale energy costs.

Unlike existing homes retrofit, establishing such a target would be a zero-cost demand reduction measure for Government as it would simply raise the bar for all housebuilders ensuring a level playing field for the market.

EPC A homes energy costs are on average half of those of EPC C, the current Government target for all homes. While EPC C is a viable target for upgrading the UK's existing stock it is too low a standard for new build especially taking into account that modular housing can deliver high numbers of low carbon EPC A stock at competitive price points today.

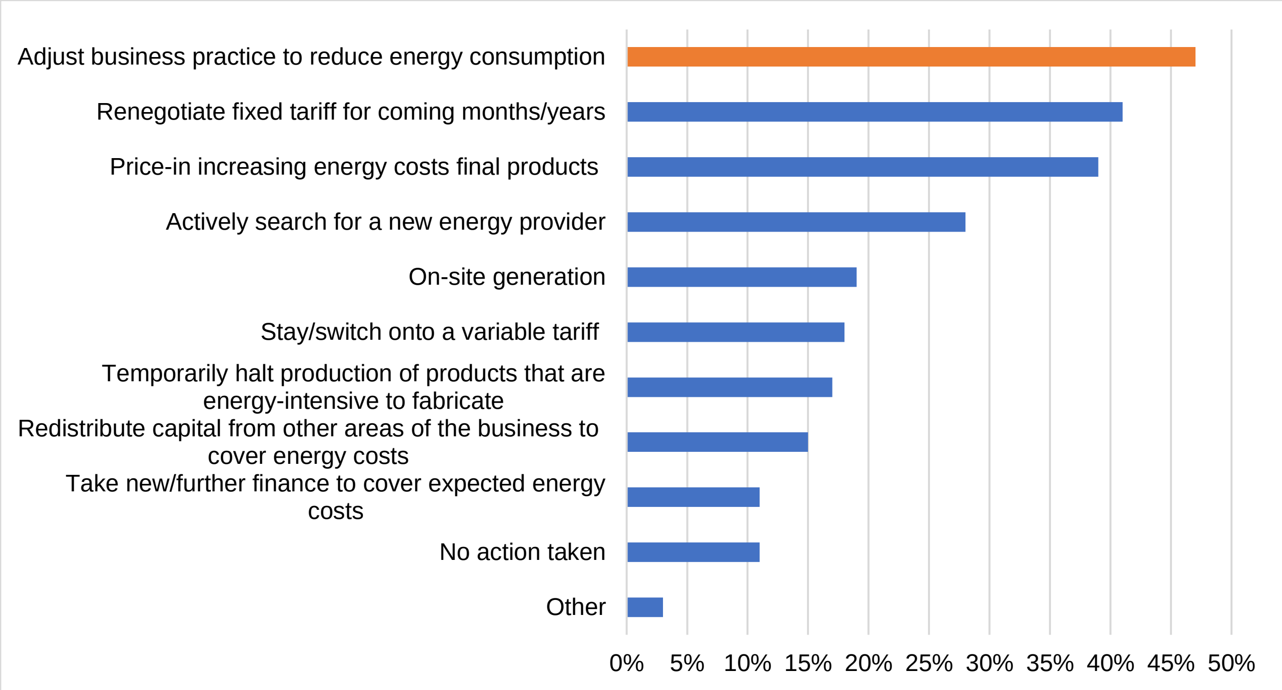
Modular products like Ilke Zero via which consumers are expected to pay nothing for energy, saving nearly £1,000 a year on bills, are in place now. Putting in place higher energy performance standards for all new build homes will accelerate the delivery of high quality, low energy modular housing helping to transform the marketplace and deliver crucial demand reduction for domestic energy.

14. While energy prices had been increasing in the background for a little while before the turn of the year, for many in the industry, their first exposure to these new heightened costs came when their current energy contracts expired, and the time came for renegotiation. This coincides with our research which found the top action taken was to adjust business practice to reduce overall energy consumption. Moreover, manufacturers are set to be exposed to a sudden and sharp increase in their energy bills when they renew their energy contracts fixed at an agreed price this Spring or the Autumn.

15. While the immediate response might be to insulate buildings and install better performing heating systems or even look to self-generate, manufacturers may struggle to access the funds and finance needed to take this course of action. The only option left for many companies will be to recover increased energy costs

by passing it onto the customer through an increased selling price. This would then increase UK inflation, impacting consumers who are already suffering from soaring domestic energy bills.

Chart 2: Actions manufacturers have taken in response to heightened energy prices in 2022



Source: Make UK, Manufacturing Monitor, February 2022

16. We know that the top action manufacturers are taking is to reduce overall energy consumption such as insulating buildings, installing better performing heat systems and/or moving to self-generation, but these can be costly, and businesses need support to achieve this. While the announcement to provide business rates relief to building improvements is welcomed, more action is needed to incentivise investment in energy efficiency measures.

17. Government should immediately reform the Industrial Energy Transformation Fund (ETF) by increasing the funding available, extending its eligibility to more energy users and reducing the criteria to ensure access to all energy users. In addition, the Government can tackle the policy costs associated with electricity prices. Many of the measures Government could take are compensation or exemption based rather than providing subsidies.

18. With immediate effect Government should:
    - **Reduce the carbon price via the cost control mechanism within the UK ETS** providing immediate support for all manufacturers.
    - **Remove the additional Carbon Price Support (CPS) tax** that only UK consumers pay, which would drive down the electricity price.
    - **Consider removing the Climate Change Levy** entirely to further reduce costs.

19. For Energy Intensive Industries the Government can go further and:
    - **Increase the relief from the Renewables Levies** now that the UK is no longer subject to EU State Aid rules.
    - **Increase compensation for the indirect cost of carbon**, benefitting the most trade-exposed and energy-intensive industries.
    - **Implement network cost reductions** for the most electro-intensive industries.

Reintroduce trade credit reinsurance as well as liability holidays for those companies straddled with debt.

20. Alleviating debt pressure from those businesses who find themselves still under its weight at the end of 2022 will be critical in ensuring sections of the industry aren't left behind, particularly as the industry's recovery is slower in subsectors, such as automotive and aerospace. Further payment holidays for those straddled with debt right now, especially within those now slower recovering subsectors is needed.

21. The Chancellor's announcement of the Pay as You Grow scheme provided much needed breathing room for those businesses who were struggling with their liabilities having taken on extra debt in the pandemic. The loan term extension was a much-used feature by manufacturers, therefore offering an additional loan payment holiday for those struggling businesses right now could support businesses with crippling costs. The scheme offered should continue to be a loan term extension at the same fixed interest rate, with options for interest-only payment periods and the option for a single repayment holiday.

22. The trading environment is still likely to be irregular right the way through to 2023, and manufacturers risk having already used their 'wildcard' holiday in 2021, leaving them exposed to their debt pressure with less recourse. That's why our research shows, payment terms and non-payment are of paramount importance to manufacturers' cash flow, but for the industry to maximise its recovery potential it needs to be trading globally. Especially where new international customers are concerned, the security provided by trade credit insurance schemes can bolster businesses willingness to seek new trade opportunities, with the knowledge that their liquidity is insured in case of non-payment or non-delivery.

Encouraging capital investment

Extend the Super Deduction scheme with a view to making it permanent at the Autumn Budget.

23. At the time of the Chancellor's Super Deduction announcement, 50% of manufacturers said the introduction of the Super Deduction will have no impact on their investment plans. Of those that did intend to use it, 23% said they will be increasing their total level of investment, and 28% said they would bring forward their already existing investment plans to take advantage of the scheme[4]. Those businesses who have not, or intended not to use the scheme commonly cite some or all of the following reasons as to why:

    - Exclusion of leasing
    - Exclusion of used/second-hand
    - Investment plans are too rigid
    - Lack of investment capital/ low spare capital due to Covid
    - Lack of confidence/ do not want to commit capital during the pandemic

24. However, it was clear that manufacturers were using the scheme with the median investment value being £228,500. As a result, the Super Deduction policy should be re-announced with a significant extension, so that industry can effectively plan investment in the medium to long term, moving it away from a short-term Covid intervention policy. Furthermore, the industry has become increasingly cautious over the last two years of spending capital, especially given the continued input price pressures the sector is facing, and will likely continue to face, for the rest of 2022. As a result, the Chancellor should look to make the modified Super Deduction permeant at the Autumn Budget.

25. SMEs take more time to digest new policy tools that may be of benefit to them as often owner managers rely on their small finance and accounting department to investigate returns on investment[5]. If they do not have their own finance department, then they would need to outsource the service to expensive external consultants. In comparison, larger manufactures have more resources to devote and find it easier to make quick turnarounds on short-term policies. For example, 45% of SME manufacturers are not aware of the super-deduction scheme, which is greater than the overall manufacturing average of 32% highlighting that larger businesses engage faster with new policy tools.[6] An extension to the super-deduction scheme would result in greater benefits for the SME manufacturing community.

26. In addition to the super-deduction extension, to ensure all possible avenues of investment incentives are covered for manufacturers, the Annual Investment Allowance (AIA) upper limit of £1m (which currently ends in March 2023) must also be extended for a significant period to allow manufacturers to plan ahead. Manufacturing businesses often make substantial productivity enhancing investments over 5–7-year cycles and therefore any investment incentive that currently exists should be designed with a longer-term view. The risk of not doing so can result in greater investment in low value-added capital rather than productivity enhancing ones.

[4] Make UK, Manufacturing Monitor, February 2022
[5] SMEs are defined as less than 249 employees
[6] Make UK, Start up to Scale Up: Supporting SMEs to Grow, December 2021

Tackling labour shortages

Introduce an Employer Training Fund to support businesses and workers to reskill and upskill.

27. Access to the right skills is a critical priority for manufacturers in 2022. This extends beyond recruiting new talent into retaining the people they already have; around 80% of manufacturers are concerned about skills leaving their business this year and are increasingly prioritising staff retention. While the Government is currently consulting on the details of its proposed Lifelong Loan Entitlement to cover short-term modular learning between levels 4 and 6 over an eligible adult's lifetime, this policy will not come into effect until 2025 at the earliest. Measures which have been financed through the National Skills Fund such as Skills Bootcamps and free level 3 courses are also welcome, but more can be done.

28. Given the high priority attached by employers to retraining and upskilling, there is a strong case for action now to support employers to continue developing their workforce. The Government should introduce an Employer Training Fund to support businesses and workers to reskill and upskill. This would allow employers to reclaim a portion of the cost of training of existing employees, making it easier and more affordable to equip their workforce with the skills needed for the future, at a time when rising costs elsewhere risks this essential investment being deprioritised. The Government should explore whether provision could be made through the Adult Education Budget to establish the Employer Training Fund as a minimum three-year programme for employers to access subsidised skills training, until the Lifelong Loan Entitlement becomes available to eligible adults in 2025.

Instruct the Migration Advisory Committee to review the shortage occupation list and introduce an emergency temporary visa route

29. In addition to retaining and upskilling their existing workforce, manufacturers need access to the right skills now to ease the current impact of labour shortages. The HGV driver crisis last year has shown that the new points-based immigration system needs to be made more dynamic and responsive to employer demands. In particular, the new skilled worker route – including the shortage occupation list, which removes some of the administrative and financial burden of recruiting from outside the UK – should ensure that manufacturers can bring in the talent they need from overseas.

30. The shortage occupation list has not been fully reviewed since 2020, in the first months of the COVID-19 pandemic and prior to the introduction of the new points-based system. Therefore, the current list is significantly out of date and does not provide an accurate reflection of where employers are currently struggling to recruit from the domestic labour force. It is essential that the Government commissions a full review of the shortage occupation list and acts upon the recommendations of the Committee to ensure that businesses can access the skills they need. The length of time between future reviews should also be shortened in order to keep the list up to date.

31. In some cases, businesses in the manufacturing and engineering sector are unable to recruit the labour they need from overseas through the skilled worker route, despite roles requiring a high level of technical skill. An example of this is the Electroplaters category, which contains job roles requiring skilled candidates where employers are unable to recruit domestically to fill long-standing vacancies. The Government should expand the occupations eligible for the skilled worker visa. They should review the roles which are currently ineligible for the skilled worker route and ensure that employers are able to recruit from overseas where it is not possible to fill vacancies domestically.

32. Creating an emergency temporary visa would help employers to recruit more quickly and efficiently from overseas at times of very high demand. In having already established temporary flexibilities for specific sectors to reflect short-term or seasonal business changes, the Government has demonstrated that the points-based system can accommodate urgent employer demands. An emergency temporary visa would extend this approach and help to minimise future disruption in critical sectors like manufacturing and their supply chains.

Cutting red tape

Further extension for CE marked products to be sold on the UK market for products where the legislation in the UK remains the same as in the EU.

33. While Make UK is not against regulating differently from the EU particularly in new technologies and cutting-edge processes, it's important to recognise that any divergences in legislation have the potential to create a non-tariff barrier without significant benefit. It is important therefore for the UK to pursue, where possible, mutual recognition agreements but also to consider from a UK perspective whether legislative changes can be mirrored to ensure that products remain compatible with both market legislations. In the absence of these agreements the UK Government should consider, for manufactured goods, that CE market goods which meet EU rules which are similar or identical to UK market rules should be continued to be accepted on the market.

34. This easement should be extended for as long as required for each product category and certainly until there is a potential divergence between UK and EU rules. The easement would significantly reduce a significant cost burden on industry at a time when UK business is faced with unprecedented increase in costs, particularly in the price of energy. Added burdens from cost and administrative requirements on placing goods on the GB market, will be a deterrent on international businesses selling into GB, add to the cost pressures on domestic business activity and limit good availability and choice on the GB market. For the UK to be an open economy, to trade successfully and boost the appetite for GB and global firms to regain confidence in international trade, an extended easement period on the introduction of UKCA is vital.

Extend the Export Support Service remit to support businesses in the importing of goods to the UK.

35. Make UK has welcomed the continued easement of the SPS control on food imports, addressing concerns about the readiness of both UK firms and international suppliers. However, there has been a mixed response from many large food manufacturing businesses who have already invested significantly to ensure they were ready for the changes and see the extension of the easements on UK import border controls as putting UK firms at a competitive disadvantage to EU firms. Make UK also welcome the establishment of the Export Support Service as a one stop shop for exporters, and particularly the support for exporters impacted by the conflict in Ukraine. While some predictability had started to return to cross border trade with the EU, companies do believe that the new customs and border formalities have affected their relationship with the EU. This includes many small businesses who see this as an ongoing challenge. With the changes to the UK Border, uncertainty about the impact of the conflict in Ukraine, many businesses still need further support.

About Make UK

Make UK is backing manufacturing – helping our sector to engineer a digital, global and green future. From the First Industrial Revolution to the emergence of the Fourth, the manufacturing sector has been the UK's economic engine and the world's workshop. The 20,000 manufacturers we represent have created the new technologies of today and are designing the innovations of tomorrow. By investing in their people, they continue to compete on a global stage, providing the solutions to the world's biggest challenges. Together, manufacturing is changing, adapting and transforming to meet the future needs of the UK economy. A forward-thinking, bold and versatile sector, manufacturers are engineering their own future.

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