

Chancellor went for the wrong tax

A letter to the Herald, November 2008

Sir -

In these difficult times everyone agrees that the economy needs a very significant boost, though opinion varies on how best to boost it.

Whatever your view on the merits of a big short term tax cut giveaway, it is bizarre that the government have chosen to do it by cutting VAT. I fear that what this really gives away is the danger of having a government with so little first hand experience of business.

They seem to believe that the change will lead directly to an equivalent drop in prices, stimulating a spending boom, and all taking effect within six days, by 1st December.

This is just not the way many consumer-facing firms set prices. True, the move gives companies another couple of points of margin to play with, and some will go on price cuts. But many retailers are already discounting heavily anyway; this is unlikely to make a significant difference there. If you are charging £5.99 for something you don't necessarily change the price to £5.86 just because the VAT rate has changed.

In any case, many firms would struggle to change prices so quickly. And it can be prohibitively costly to re-print menus and especially mail order catalogues. Supermarkets could respond very quickly, but there's no VAT on the food they sell anyway.

The Chancellor has taken an enormous gamble with a £20bn giveaway now and a £40bn takeaway later. Of course we all hope that the 'stimulus package' does what he says it will. But the danger is we end up with all the pain for only part of the gain.

Yours

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