Predictions for business and politics in 2018

INTRODUCTION

At the beginning of last year, the IoD made five predictions about economics and politics over the next 12 months:

- Theresa May will trigger article 50 in 2017
- UK tax revenues will continue to disappoint
- Populist revolts are far from over
- A significant cyber-attack will bring down a company
- European banks are in serious trouble

Our record wasn't bad. Some predictions, such as that the Prime Minister would start the Brexit countdown, were delivered quickly (although it's easy to forget now, this was not a forgone conclusion – the Supreme Court was still deliberating on whether Parliament needed to approve Article 50 in January).

Others were borne out, if not universally, then in notable examples. While economic growth improved appreciably in the EU in 2017, concerns about banks in several countries remain. In the most high-profile case, Monte dei Paschi di Sienna, the world's oldest surviving bank, had to be bailed out by the Italian government to the tune of €5.4bn.

Populism was very much on display in 2017. While Emmanuel Macron fought off the challenge of the National Front's Marine Le Pen, in Germany the far-right AfD entered the Bundestag as the third largest party. By one measure, the number of populist parties in Europe has almost doubled from 33 in 2000 to 63[1].

Cyber attacks continued to engulf global companies, with Uber, already fighting fires on a few fronts, taking a serious reputational knock when it was revealed in November that not only had it suffered a massive hack that had exposed the data of 57 million users and drivers, it had also initially attempted to brush the incident under the carpet by paying off the criminals and keeping the information from regulators. The subsequent contrition of the new CEO, Dara Khosrowshahi, only goes to prove how worried executives are, and should be, by cyber risks.

Tax receipts have fared better than we expected, up 6.8% between 2015/16 and 2016/17. At the November 2017 Budget the Office for Budget Responsibility revised up their forecasts for tax receipts for 2017/18, but they expect growth to be slower in subsequent years.

This year, we are taking the brave (or foolhardy) step of making predictions across several different areas that relate to business, 14 in total. It will be a year of great change for companies, characterised by both uncertainty and determination to succeed. Half of IoD members say they are optimistic for their own business in 2018, but less than a quarter say the same for economy as a whole. Our members are hoping for continued progress in the Brexit talks and, at home, the Government's Industrial Strategy to bear fruit. Many will be hoping for a year free of too many political surprises, but that is one prediction we are not willing to make.

ECONOMY

1) London's economic growth will be weaker than the UK average in 2018

This would buck a long-term trend that has seen London consistently outperform other UK regions. Uncertainty around Brexit, particularly regarding financial services and access to skills will disproportionately weigh on the City – as will weaker consumer spending. Meanwhile strength in manufacturing activity – owing to the weak currency and global growth – will provide some buoyancy for the regions.

---

[1] Research conducted by the Tony Blair Institute for Global Change, available at: https://institute.global/insight/renewing-centre/european-populism-trends-threats-and-future-prospects

2) Business investment growth will fall short of official forecasts for 2018

Our members' investment prospects for the year ahead have been subdued, largely due to political uncertainties. But also, elevated costs, absorption of additional labour market capacity, and redirected revenues (for contingency planning, product launching etc.) will weigh down investment in capital and technology. As a result, business investment growth next year will likely lie closer to 1.5% – short of the Office for Budget Responsibility's 2.3% forecast – before rebounding in 2019.

CORPORATE GOVERNANCE

3) Global stock markets will come under growing pressure to relax their listing rules, as competition for major flotations hots up

In 2017, the New York Stock Exchange has overtaken Hong Kong as the top global venue for companies undertaking initial public offerings. This reflects a surge in the number of Chinese companies that have chosen to list in New York rather than Hong Kong. One of the reasons underlying this trend is that the NYSE allows listing of shares with multiple voting right (in contrast to Hong Kong, Singapore and London). Such shares are heavily used by tech entrepreneurs who want to raise funds without ceding voting control to other shareholders. Growing competition amongst stock exchanges will tempt other markets to relax their listing rules in a similar direction, with potential implications for global corporate governance.

4) Several major UK companies will appoint employee representatives as board members for the first time

Although common in continental Europe, the presence of employee representatives on UK boards is a rarity. However, proposed reforms to the UK Corporate Governance Code seek to give an increased voice to employees and other stakeholders in corporate governance. Reflecting this development, several major UK companies will appoint employee representatives as board members for the first time in 2018, although the practice will remain relatively unusual due to the strong shareholder orientation of most UK enterprises.

EMPLOYMENT

5) Legal challenges against gig economy platforms will keep rolling

The gig economy will stay a controversial subject with trade unions taking more online platforms to court to challenge their work policies. High profile legal disputes have underlined the ambiguous definitions surrounding employment status in the UK. The issue has proven a challenge for legislators, and it's incumbent on Government to provide clarity for businesses moving forward. The situation is unlikely to be totally resolved in 2018 and controversies and contentious court cases will continue to be the order of the day.

6) Net migration will continue to fall

Net migration to Britain will fall by at least 50,000, bringing the Government the closest they have come to reaching their net migration target since it was first introduced in 2010. Though the rights of EU citizens in the UK were recently firmed up in Brexit negotiations, EU inward migration will continue the decline it has taken since the referendum. As a result, businesses – particularly SMEs – will find it more difficult to recruit the people they need for our economy to prosper resulting in a labour market tightening. Some firms will feel pressure to raise wages but others will struggle to cope and will consequently stagnate or downsize.

TAX

7) The Treasury will try to tax the self-employed more like employees

The different treatment of employees, contractors and the self-employed when it comes to Income Tax and National insurance has been brought to public attention by the rapid growth in the flexible economy. The area is politically challenging because, although most people in work are disadvantaged by the current treatment as they pay income tax and national insurance under PAYE, there is a vocal minority who could be required to pay higher national insurance contributions (and, at the margin, more income tax) if changes are implemented. The Government has been cautious so far, excluding tax policy from Matthew Taylor's recent review of modern employment. Rather than make sudden changes, we predict the Chancellor will launch a consultation at the Autumn Budget, putting forward several options for reform.

8) The Government will launch a review of business tax reliefs - and find they are worth keeping

There have been increasing calls recently for cuts to tax reliefs in areas like start-up investment. We believe these calls should be resisted for several reasons. Firstly, who receives tax relief matters less than the behaviour secured. Secondly, calculations of 'tax expenditures' often include both capital and annual investment allowances, but these represent the tax approach to providing – and controlling – the allowance for capital expenditure. Without these reliefs, the effective rate of tax on profits would be above the rate enacted by Parliament. Thirdly, equating 'tax expenditures' with public spending leans on the false assumption that all income belongs to the state. We predict that the Government will, correctly, maintain all significant reliefs in broadly their current form for 2018.

TRANSPORT AND COMMUNICATIONS

9) Mobile and broadband data consumption will grow by at least another 30% in 2018.

This rise will be driven by video streaming and cloud-based services which will stretch the UK's telecoms networks to their limits. This will put greater pressure for a more radical intervention by the government with the forthcoming review of the Telecoms market announced as part of the Industrial Strategy. Openreach will feel obliged to offer more ambitious fibre to the premises plans while faster, nimbler Alternative Network Providers continue to attract new waves of investment.

10) The first people will fly from a reusable suborbital space vehicle

In doing so, Blue Origin's New Shepard will open up a brand new market for space tourism, remote sensing and observation, and scientific research. The UK will then push harder to attract a working operator to one of the shortlisted potential spaceports. Meanwhile, reusable rockets as pioneered by SpaceX will start to look normal.

EUROPE AND TRADE

11) There will be written commitment to a transition deal by March

Now that phase one issues have reached 'sufficient progress', it's vital the Government reaches swift agreement with the EU on transitional arrangements for Brexit. While companies are keen to know what the terms of the final deal will be, the more urgent matter is detail of the implementation period. In essence, UK businesses leaders want to know the realities of trading on exit day in March 2019.

Given the tight timeframe and urgency of transition for businesses, the simplest arrangement would involve the continuance of the status quo - both in terms of Single Market access and Customs Union membership - for the duration of the bridging period. In doing so, the Government would show it is taking heed of calls from the business community that the process of exiting the EU should only involve one set of adjustments. It is by no means certain, but we predict a political agreement between the UK and the EU on the terms of transition will be reached by March.

12) The ground will be prepared for future regulatory cooperation

One of the most important discussions for phase two is to what extent UK regulation diverges from the EU after Brexit. The question brings to light a central trade-off: while more flexibility in setting regulations could help in future trade deals outside the EU, UK businesses want to avoid barriers that make trade with the EU – our biggest and closest trading partner – more challenging. Our prediction is that this question will not be resolved in 2018, the UK Government will instead focus on the near-term, putting mechanisms in place that facilitate regulatory cooperation with the EU for the period immediately after Brexit.

TECHNOLOGY AND ENTREPRENEURIALISM

13) Digital giants will come under sustained pressure to stamp out fake content on their platforms

The use of social media as a platform for accessing news content has continued to grow particularly in both the UK and the USA over the past year, exacerbated by deepening political divides and low trust in established media sources. According to Reuters, 4 in 10 UK residents now use social media as a news source. Set against this backdrop has been a spate of fake news controversies which – by the time they have been disproved – have already reached their intended audiences. With suggestions already in place in the UK for a tax on firms that fail to tackle terrorist content in good time, fake news will not be far behind.

14) The number of companies being formed will continue to rise

The UK landscape for entrepreneurship will remain robust in 2018. According to the IoD's latest survey on start-up confidence, UK entrepreneurs are coming into 2018 with a positive attitude towards jobs and investment in their firms. At the same time, the UK's ranking in the Global Entrepreneurship Index has jumped from 8th in 2017 to 4th this year. With these favourable tail-winds, we are confident that UK start-ups are well-placed to take another year of political uncertainty well in their stride.