The Big Buyback

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Introduction

Among the many giveaways to the wealthy featured in Kwasi Kwarteng’s mini-budget, one that has received less attention is the reversal of Rishi Sunak’s 1.25 percentage point increase of tax on individuals’ dividend income, thereby bringing the basic and higher rates back down from 8.75% and 33.75% to 7.5% and 32.5%, respectively. In contrast with the Chancellor’s U-turn on his attempt to remove the additional 45% rate band for income tax, these cuts appear to be going ahead unchallenged. The top rate on dividend income (equivalent to the 45p band for income tax) currently taxes dividend income at 39.35%, following the 1.25% increase effective as of April 2022. Given the current Chancellor’s U-turn on abolishing the top rate of income tax, this implies the top rate for dividend income will presumably now be lowered back to 38.1%, eliminating Rishi Sunak’s short-lived uplift.

Compared to the extraordinary size of the overall policy package announced in the mini-Budget (with the proposed elimination of the top band carrying a £2 billion price tag on its own), the £600 million cost of the 1.25 percentage point dividend tax cut may well appear relatively small. It does, however, offer an insightful suggestion of what the Chancellor believes is holding back the UK economy, and what exactly he believes must be “unchained” in order for the “growth engine” to roar back to life.

Despite recent rhetoric from the government claiming that growth has taken a backseat to “redistribution” for the past decade, several recent studies point toward an economy in which corporate cash has increasingly been funnelled back to shareholders at the expense not only of workers, but also of the productive investment needed to undergird economic growth. Given that dividends already receive preferential tax treatment, and with an eye toward who stands to benefit most from these changes, it is unclear through what mechanism the Chancellor expects his tax cuts to foster innovation and entrepreneurial risk-taking.

Who Benefits?

Dividend income is already subject to a £2,000 tax-free allowance where none existed before 2016 and enjoys far lower marginal rates than labour income.

With respect to sources of household income in the UK, dividend income is barely 6% the size of employee compensation. Thus, the £2,000 allowance for dividend income is extremely generous relative to the £12,570 allowance for income tax as a whole, though admittedly not as extreme the £5,000 allowance initially introduced by George Osborne in 2016. And while there is no publicly available data on the distribution of dividend income, there is for direct ownership of UK shares (albeit not for non-UK shares). Figure 1 shows the average value in GBP of household UK share ownership for each income decile as of 2016-18, with the top decile also broken down into the top 1% and top 0.5%.

In line with this distribution, assuming for argument’s sake a dividend yield of 4% (the prevailing yield on the FTSE 100), then the highest earning 0.5%, of whom only half hold shares, would receive £44,600 a year per household. Share-holding households within the next 0.5% would receive £8,400 — within the rest of the top decile, £3,000. In no other income bracket would the average share-holding household clear the £2,000 allowance in order to benefit from the Chancellor’s handout (based on UK shares alone.

Figure 1 Direct ownership of UK shares across the household income distribution

Note Figures reflect the total value of shares held in a given income decile divided by the total number of households in the decile. Note that the Top 1% and Top 0.5% shown above are subsections of Income Decile 10 (Highest).

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6. See https://www.dividenddata.co.uk/ftse-index-yield.py
Dividends and Household Income

Previous Common Wealth research noted how dividend payouts by UK private non-financial corporations have far outpaced wages over the two decades up to the pandemic, based on ONS data from the UK Economic Accounts.\(^7\)

Recent quarters have told a more moderate story on the corporate side, with the pandemic setting the ratio of dividends to total labour compensation roughly back to its 2012 level, and the ratio of profits (measured by gross operating surplus) to labour compensation to its 2010 level. No reversion to the old trend has yet occurred.

From the perspective of household income, however, dividends are buoyant. Figure 2 compares the trajectories of household labour income and dividend income (as well as non-financial profits) relative to their 2010 levels. Volatility notwithstanding, the pattern is clear. Aggregate household dividend income has grown more than 100% in nominal terms since 2010, while labour compensation and corporate profits have each grown by less than 50%.

![Figure 2](https://www.common-wealth.co.uk/upload/figure2.png)

**Figure 2** Household income: dividends vs pay

**Note** Aggregate nominal figures are indexed to their 2010 levels to highlight change over time. Shaded columns represent periods of Covid-related national lockdown.

FTSE Kickbacks

While the corporate dividend payments reported by the ONS show that the split in the proceeds of growth between labour and shareholders has been much more acceptable in recent quarters than in the preceding two decades, the picture is less

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benign when we look at FTSE-listed firms. Where the UK Economic Accounts is restricted to all “resident institutional units”, including privately traded firms, the FTSE comprises a narrower set of publicly traded companies, but many of whose activities are global in scale.

Among firms currently listed in the FTSE All Share, dividends have been steadily climbing relative to relative to labour costs during the decade from the Great Recession to the Covid pandemic, peaking in 2019 at £28 bn per quarter relative to just £17.3 bn in 2014. After a mid-pandemic dip, dividends have returned to their 2017-18 level (they were already recovering even as the third lockdown bit in early 2021). This recovery does not appear to have been matched by a similar recovery in labour costs, though we still lack data on recent quarters.

The more dramatic story has been share buybacks, which, as a form of shareholder payout, are functionally identical to dividends but qualify for more generous tax treatment as a capital transfer. While typically smaller in scale than dividends, they have become the main margin for rising shareholder payouts, especially in the last year as profits have witnessed an extreme spike. From a 2015 average of £3.4 bn per quarter they more than doubled to £8.2 bn by 2019. Buybacks in 2022Q2 have reached £16.2 bn among those firms to have filed results so far, up from £5.1 bn one year earlier, and a 2019 quarterly average of £6.4 bn.

Figure 3  Shareholder payouts vs. labour costs before and after the pandemic

Note  Annual aggregates are used for 2014-19 to smooth out uninformative fluctuations. Quarterly data from Q1 2020 onwards is then presented, annualised for visual consistency. Due to data limitations, labour costs are not shown beyond Q3 2021.

The post-pandemic explosion in shareholder payouts has been driven overwhelmingly by extractive firms in industries such as commodity mining and oil
and gas, as research by Common Wealth and IPPR has previously laid out in detail. Historically, industries such as real estate and information technology have been the most remunerative. The thread that runs through all of these is ownership of scarce assets — and how that is translated into handsome reward for shareholders. Juicing the rewards of such ownership will not make the economy more productive, nor will it solve the corrosive underlying combination of inequality and stagnation holding back the UK economy.