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Autumn Statement 2013

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The Treasury Committee

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1 Introduction

Our inquiry

1. The Autumn Statement was delivered by the Chancellor on Wednesday 5 December 2013, and the *Economic and fiscal outlook* was published by the Office for Budget Responsibility (OBR) on the same day. In examining the policies and forecasts presented in these documents, the Treasury Committee held four oral evidence hearings, during which we took evidence from six panels of witnesses as follows:

Monday 9 December 2013: Office for Budget Responsibility

Robert Chote, Chairman, Graham Parker, Member, and Professor Stephen Nickell, Member, Budget Responsibility Committee.

Tuesday 10 December 2013: City Economists

Brian Hilliard, Chief UK Economist, Société Générale, Alan Clarke, Director, Fixed Income Strategy, Global Banking and Markets, London, Scotiabank, and Melanie Baker, Vice President, UK Economics, Morgan Stanley.

Thursday 12 December 2013: HM Treasury

Rt Hon George Osborne, Chancellor of the Exchequer, and Mr James Bowler, Director for Strategy, Planning and Budget

Tuesday 17 December 2013: Experts and interested parties

First Panel: Paul Johnson, Director, and Carl Emmerson, Deputy Director, Institute for Fiscal Studies;

Second Panel: Paul Smee, Director General, Council of Mortgage Lenders;

Third Panel: Stephen Glaister, Director, RAC Foundation, and Peter Atherton, Equity Research, Liberum Capital.

We have also made use of oral evidence into the Bank of England Monetary Policy Committee's November 2013 Inflation Report, given on 26 November 2013. The Committee is grateful to all those who gave their time to provide oral evidence to us, in some cases at short notice.

2 The macroeconomy

Recovery

2. There has been an improvement in the near-term outlook for the economy since the OBR's last forecast in March 2013. As Table 1 shows, the OBR now forecasts stronger GDP growth in 2013 and 2014. This forecast improvement in the near-term outlook followed improved forecasts for UK growth by the IMF in October 2013 and the OECD in November 2013.[1] Unemployment has fallen from 7.8 per cent in Jan-Mar 2013 to 7.2 per cent in Oct-Dec 2013.[2] In the minutes of its December 2013 meeting, the Monetary Policy Committee of the Bank of England also provided evidence of a recovery:

> The news on the month had continued to suggest a burgeoning recovery in the United Kingdom. The second estimate of GDP growth in the third quarter had been unrevised at 0.8 per cent. Business surveys pointed to growth rates of around 1¼ per cent in each of the next two quarters, and although Bank staff took a more cautious view they nevertheless expected growth of 0.9 per cent in the fourth quarter of 2013. The recent data suggested that the recovery was being driven by consumption and stockbuilding, with both investment and net trade weaker than expected, although the Committee treated first estimates of the GDP expenditure breakdown with considerable caution.[3]

Table 1: OBR GDP growth forecast (in per cent)

At:	Outturn	Forecasts				
	2012	2013	2014	2015	2016	2017	2018
March 2013	0.2*	0.6	1.8	2.3	2.7	2.8	
December 2013	0.1	1.4	2.4	2.2	2.6	2.7	2.7
Change	-0.1	0.8	0.6	-0.1	-0.1	-0.1	

Source: Office for Budget Responsibility, Economic and Fiscal Outlook, Cm8748, December 2013, p10, Table 1.1; Office for Budget Responsibility, Economic and Fiscal Outlook, March 2013, Cm8573, p9 , Table 1.1

**Forecast*

Revisions by ONS in December 2013 also showed that GDP in 2013 had been stronger than originally estimated. The ONS reported that "GDP in volume terms increased by 1.9 per cent when comparing Q3 2013 with Q3 2012, revised up 0.4 percentage points from the previously estimated 1.5 per cent increase."[4] It also noted that "In Q3 2013 GDP in volume terms was estimated to be 2.0 per cent below the peak in Q1 2008, as compared with 2.5

1 IMF, World Economic Outlook: Transitions and tensions, October 2013, Table 1.1, p2; OECD, Economic Outlook, Volume 2013/2, November 2013, p120

2 ONS, Labour Market Statistics, February 2014, published 19 February 2014, Table 1

3 Bank of England, Minutes of the Monetary Policy Committee meeting held on 4 and 5 December 2013, published 18 December 2013, para 21

4 ONS, Quarterly National Accounts, Q3 2013, 20 December 2013

per cent below this peak as previously estimated."[5] The latest ONS GDP estimate for 2013 Q4 stated that "GDP remains 1.4% below the pre downturn peak".[6]

3. Recent survey data has also been positive. As the Office for Budget Responsibility noted in its Economic and Fiscal Outlook:

> Most survey evidence suggests a strong pick-up in underlying activity in recent months. In October, the composite CIPS Purchasing Managers' Index (PMI) rose to its highest level since May 1997, 7.1 points above the series average of 54.0. The PMIs for manufacturing, construction and services are all well above the average of recent years, although the manufacturing index fell back slightly in October. The construction PMI has been lifted by the housing sector; the sub-index has risen 8.6 points since its recent trough in June 2013.
>
> The Bank of England Agents' Summary reports a sustained increase in investment intentions and exports of goods as well as stronger demand for consumer goods and services since the time of our March forecast. The GfK Consumer Confidence measure suggests that consumer sentiment has risen since March and returned close to its long-run average after nearly 6 years running below it. Within this measure, there has been a significant improvement in the climate for major purchases and in expectations for the general economy. The Confederation of British Industry's (CBI) quarterly Industrial Trends Survey reported that growth in manufacturing output and new orders for the second and third quarter of 2013 were both stronger than their long-run averages. The CBI's Service Sector Survey reported business volumes in the three months to November increasing at their strongest pace since 2007. [7]

In January 2014, the BDO Optimism index rose to the highest level since the index began in 1992.[8]

4. Robert Chote, Chairman of the Office for Budget Responsibility, provided the following outline of the drivers of this near-term recovery:

> If you look at the surprise we have had in the data since the Budget then the main contributors to the fact that the growth has been stronger than we anticipated are consumer spending, private consumption and the housing market. Net trade and business investment continue to disappoint. On the consumer spending side, it does seem to be that it is people dipping into savings or taking more debt rather than an increase in income. As we know, real incomes remain very weak. Looking at that element, you can see that that is what appears to be driving the most recent news.[9]

However, in its Economic and Fiscal Forecast, the OBR provided the following warning:

5 ONS, Quarterly National Accounts, Q3 2013, 20 December 2013

6 ONS, Second Estimate of GDP, Q4 2013, 26 February 2014 , p3

7 Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 8748, December 2013, p21, para 2.8

8 BDO, BDO Business Trends, 13 February 2014

9 Q6

> We are conscious that forecast revisions tend to lag economic developments at turning points, leading to repeated overestimates of economic activity in downturns and repeated underestimates when activity finally picks up. But the experience of 2010 provides a recent example of what appeared to be a turning point in the cycle ebbing as the factors needed to generate self-sustaining recovery failed to take hold. And with productivity, real income growth and UK export markets remaining weak, and problems in the euro area far from fully resolved, our central forecast—like that of the Bank of England—does not assume that the growth rates seen in the last couple of quarters are maintained through next year and beyond. We assume that growth slows to rates of around 0.5 per cent a quarter through 2014, with risks to both the upside and downside.[10]

The Monetary Policy Committee also provided a similar warning in the minutes of its December 2013 meeting, noting that for a recovery to be sustained, it would have to be seen in more sectors of the economy:

> A sustained recovery was likely to require a pickup in investment growth as well as consumption, and some rebalancing from domestic to external demand. The prospects for continued robust consumption growth would depend on productivity gradually increasing and supporting a strengthening in real incomes. There had been some signs of softness in recent consumer spending data and confidence surveys. However, there were increasing signs from business surveys and the Bank's Agents that investment might be rising as expectations of a continued recovery in demand became entrenched. The net trade data had been weak over the past couple of years, reflecting in part demand conditions in the rest of the world. In the euro area, only a very weak recovery was in prospect and inflation remained materially below 2 per cent, but a moderate expansion appeared to be underway in the United States and there were signs that growth in the emerging economies had bottomed out. It would be difficult to achieve a better balance of domestic and external demand as long as activity in the UK's main trading partners remained subdued.[11]

5. Melanie Baker, Vice President, UK Economics, Morgan Stanley, when asked whether the OBR's forecast growth rate was sustainable, told us that:

> I am confident it is sustainable, partly because I think it makes sense for the UK economy to be doing better now. Fiscal austerity is dragging a bit less this year. The external environment has improved, so the Eurozone is a bit more stable. That is important for business confidence and for the banks as well, of course. We have also seen a dramatic improvement in credit conditions. All these things mean it makes sense for the UK to be recovering. I would expect those things to persist as a central case.[12]

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10 Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 8748, December 2013, p9, para 1.20

11 Bank of England, Minutes of the Monetary Policy Committee meeting held on 4 and 5 December 2013, published 18 December2013, para 22

12 Q76

Alan Clarke, Director, Fixed Income Strategy, Global Banking and Markets, London, Scotiabank, also explained that:

> The angle I come from is it is normal to grow unless you have a countervailing influence holding you back, which we have had over the last year with tight credit conditions and headwinds from the Eurozone. It is normal to mean revert and what is the normal growth rate now? My view would be around 2 per cent or maybe slightly above that, but we have many years to go of fiscal austerity applying a brake domestically. Externally we have the brake on growth in the Eurozone from our biggest trading partner. We should move back towards trend growth, but there are a couple of headwinds getting in the way of that. The flipside is that we do have this boost coming from the housing market.[13]

Dr Carney, Governor of the Bank of England, emphasised to us that:

> When thinking about the sustainability of the recovery, we need to think about the life cycle of the recovery. Recoveries are very seldom, in this country or other countries, led by business investment. There needs to be a source of demand that then generates the need for that business investment and the confidence for that business investment. If you look at the situation the UK is in right now, that demand is not going to come from outside our shores. The eurozone has improved somewhat, but it is still very weak and growing roughly at 1 per cent a year—effectively a stagnation—and that is our largest export market, as you know. The question is the extent to which domestic demand can provide the initial lift that will bring that rebalancing towards business investment. That is what we are seeing now.
>
> What is important is that all of the elements are in place for business investment to pick up, and that means reducing unnecessary uncertainty. Our contribution to that is forward guidance, providing stimulus, again, the stance of monetary policy, but making sure that the transmission of that stimulus is as effective as possible to businesses, and that means ensuring that we finish the job on fixing the core of the financial system here, fixing the banks and major building societies, and a lot of progress has been made there. It is those elements that help put in place the conditions—demand and stimulus. They put in place the conditions for that recovery in business investment, but we still need to see it.[14]

Household consumption and household debt

6. The crucial question in current circumstances is the sustainability of a recovery based on an increase in household consumption. This is especially true against a backdrop of lower household saving and rising household debt: The IFS Green Budget 2014 notes that "there is little scope for households to reduce their savings any further",[15] and the Bank of

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13 Q84

14 Oral evidence to the Treasury Committee, Bank of England November 2013 Inflation Report, HC 825, Tuesday 26 November 2013, Q61

15 IFS, Green Budget 2014, Summary, p3

England said in its November 2013 Financial Stability Report “the UK household debt to income ratio, of 140%, remains higher than comparable ratios in the euro area and the United States”[16] We discuss these points in turn.

Household consumption

7. The OBR’s Economic and Fiscal outlook said that “With consumer spending growth forecast to outpace disposable income growth, we forecast that the saving ratio will decline gradually from just above 5½ per cent in 2013 to just under 4½ per cent in 2018.”[17] Mr Chote explained that this forecast fall in the savings ratio was because:

> Basically, you have a relatively weak process of incomes recovering. Once again, we are coming back in part to the productivity puzzle. We are still waiting for productivity growth to pick up and the expectation would be that that would lead to earnings growth. If you look in terms of real earnings, for example, we do not get the 2 per cent a year real growth in wages and salaries that people would be used to on past historical experience for a couple of years still. We have consumption rising faster than that; therefore, leading to a relatively modest fall in the saving ratio. It should be borne in mind there are other things going on within the saving ratio that means it is not quite as straightforward a picture as that, but that is broadly it.[18]

However, Mr Chote also explained that:

> People may be making their decisions on the basis of their expectations of future incomes. If there is greater optimism around about that, that could be having an impact there. The other question is whether those data remain looking as they do into the future. You will have noticed from successive ones of these that not only do the forecasts for the saving ratio move around quite a lot, but so do the estimates of its path in the past.[19]

8. The forecasts for household consumption and saving are linked to the forecast for real wages, a point emphasised by the MPC minutes for their January 2014 meeting:

> The recovery in growth over the year to 2013 Q3 had largely been driven by household spending. Following the data revisions, quarterly consumption growth over this period was estimated to have averaged 0.7 per cent, in line with its long-term average. With little growth in household income over this period, the growth in household spending had been associated with a fall in the saving ratio from almost 8 per cent to just over 5 per cent of household income. The decline in the saving ratio was likely to have reflected a number of factors including: increased optimism about future incomes; higher asset prices; reduced uncertainty and an associated reduction in precautionary saving; and increased credit availability and lower loan and deposit

16 Bank of England, Financial Stability Report, November 2013, p17

17 Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 8748, December 2013, p68, para 3.102

18 Q11

19 Q13

> interest rates. While it was difficult to estimate precisely the relative contributions of these various factors, it seemed unlikely that any would drive a similar fall in the saving ratio over the coming year. Consequently, maintaining the recent rates of consumption growth would require a sustained pickup in real income growth, preferably underpinned by stronger productivity growth.[20]

The OBR provided the following commentary on its forecast for real wage growth:

> We expect the weakness of real wage growth to persist into 2014 before picking up gradually to match productivity growth. We do not expect real take-home consumption wages to reach their pre-crisis peak until late 2015, mainly reflecting the slow recovery of productivity growth toward its historical average. With wage growth remaining weak over the near term, real disposable income is expected to pick up relatively gradually, before strengthening over the medium term as earnings growth gathers pace and inflation falls back.[21]

Given that households may be undertaking consumption now, in the expectation of rises in future income, we asked others about for their views on the future path of wages. Melanie Baker, of Morgan Stanley, explained where wage growth may come from:

> We do expect a rise in productivity. We do expect business investment to pick up. I am saying there was a bit of a pick-up last quarter, so these things should start working better, and with stronger productivity, that gives a justification for higher wage growth. You may also see pay growth for other reasons as well. The RPI rate of inflation is still relatively high. Wage demands may pick up because fears of unemployment have fallen and there are skill shortages in certain sectors as well, but average earnings growth we are expecting to pick up, but we do need to see that for a more sustainable recovery.[22]

Alan Clarke of Scotiabank noted, however, that:

> I am slightly nervous about wages. I agree the trend is favourable and it is upwards. However, what has come out in the recent labour reports is that the claimant count unemployment is going down fast, about 120,000 per quarter. There is a corresponding increase in employment, 155,000 to 200,000. Those two offset one another, but the wider definition of unemployment is going down much more slowly, even though it includes claimant count, and that is because in activity, new supply is coming into the labour pool. At the moment, that is a drop in long-term sick and discouraged workers. Further down the road, we will have Bulgarian and Romanian workers coming in, so there is obviously an increase in demand for workers, employment is going up fast, but there is a corresponding increase in

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20 Bank of England, Minutes of the Monetary Policy Committee meeting held on 8 and 9 January 2014, published 22 January 2014, para 16

21 Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 8748, December 2013, p68, para 3.101

22 Q51

> supply as well and that should slow the upward trajectory in wage inflation. I agree it should be up, but it could be perhaps a little bit slower than the OBR forecast.[23]

Commenting on both the weakness in real wage growth and how to ensure real wage growth in the future, the Chancellor argued that:

> I just think it is inconceivable that you can lose 7 per cent of your GDP and that does not have an impact on the living standards of the people of this country, but the best answer to that is to work through the problems, deal with the public finances, get the economy into a position where it can grow in a sustainable way.[24]

Household debt

9. The Economic and Fiscal Outlook forecast the household gross debt to income ratio to rise above 160 percent by 2019.[25] When asked what a high level of household debt might mean for the recovery, Spencer Dale, Chief Economist of the Bank of England, noted that:

> I think it reflects an increased vulnerability to economic shocks. The balance sheet of the household sector as a whole is relatively healthy, but within there are distributions where some people have very high levels of debt and others very high levels of savings. The vulnerability is with the people who have the high level of debt. To a very large extent those increases in debt are a counterpart to the increase in house prices we saw prior to the financial crisis, where what we saw were young households having to take out mortgages to pay for their houses. The recipients of that were old households who then saved that money, which is why the balance sheet as a whole was relatively strong but where we do have these pockets of vulnerability associated with high levels of debt.[26]

When we questioned whether households, given the level of household debt, may be vulnerable to rising interest rates, given the level of household debt, Professor Nickell, a member of the Budget Responsibility Committee, argued that:

> The rise in interest rates will stress households. The fact that a household takes on a mortgage and the mortgage and the mortgage has to be bigger than the households who were taking on mortgages 20 years ago, in some sense you could think of new mortgages replacing old mortgages and the new mortgages are going to be bigger. That is the driving force behind the rise in debt. The fundamental issue is how cautious everyone is being. Historically, people and the lenders in the UK have been reasonably cautious, which may surprise some people but is, nevertheless, true. As a consequence, the level of repossessions, as we know, has been exceptionally low relative to the depth of the recession compared with, say, the early 1990s and the level

23 Q51

24 Q216

25 Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 8748, December 2013, p70, Chart 3.24

26 Oral evidence to the Treasury Committee, Bank of England November 2013 Inflation Report, HC 825, Tuesday 26 November 2013, Q86

> of losses that lenders have made in the UK mortgage market have been absolutely tiny.
>
> You could say, "Well, yes, but there is more forbearance and interest rates are low and so on and when interest rates shoot up there will be a problem". I think it is perfectly true to say that there will be some households who will be stretched when interest rates rise, but I think we have been through this argument before. All the evidence suggests that what gets households into trouble and what leads to repossessions and so on is change in the financial circumstances of the household, either because of unemployment or because of sickness and so on, not basically because of rises in interest rates.[27]

Professor Nickell also disagreed that rising debt was the only way households would be able to sustain the economy. He argued:

> If we have productivity growth growing at its historical rate, we can easily have growth without a booming housing market. It just so happens, however, that when everyone's incomes are growing, given the desire for people to own houses and given our inability to build any houses, the inevitable consequence of that is the price of houses keeps going on up relative to incomes. If we sustain the level of owner occupation and mortgages that we have had in the last 10 or 15 years, when that happens you will find debt going up as well, but the rise in debt is not a necessarily condition once you have productivity growth and real wages growing. That alone will be quite enough to drive growth in the economy.[28]

10. On overall household debt, the Chancellor believed that:

> The best thing the authorities can do, and this is a decision that the MPC and the new Bank Governor have taken, is to at least provide people with good communication about the future expected path of interest rates. That enables families to anticipate what future changes there might be. I think the Bank of England has done a good job and indeed a better job than some central banks at giving a better forward guidance on the likely path of interest rates or the thresholds that would lead to them thinking about interest rate decisions. I think communication is an issue.
>
> I would just make this point, though. There has been a deleveraging. I completely agree with you that we had an unsustainable debt boom in the last decade that led to the biggest recession and financial crisis of modern history in this country, or contributed to it, but at the moment debt servicing costs are down for families. We also have this new architecture that will keep an eye on this and I have confidence in the system that Parliament and the Government have established to monitor this going forward.[29]

27 Q20

28 Q21

29 Q156

Trade and the balance of payments

11. The balance of payments is defined by the Office for National Statistics as follows:

> The balance of payments summarises the economic transactions of the UK with the rest of the world. These transactions can be broken down into three main accounts; the current account, the capital account and the financial account.
>
> The current account comprises of the trade in goods and services account, the income account and current transfers. A difference in the monetary value of these accounts is known as the current account balance. A current account balance is in surplus if overall credits exceed debits and in deficit if debits exceed credits.
>
> A deficit or surplus on the current account is offset with an equal and opposite surplus or deficit on the capital and financial account. As the capital account is relatively small in comparison, the current account and financial account can be said to be counterparts.
>
> The current account balance plus the capital account balance measures the extent to which the UK is a net lender (that is, in surplus) or net borrower (that is, in deficit). The UK has run a combined current and capital account deficit in every year since 1983 and every quarter since Quarter 1 2008.[30]

The persistent deficit noted above on the UK's current and capital accounts must have been offset by surpluses in the UK's financial account, which would include direct investment in the UK.

12. Net trade, defined by the OBR as "the extent to which the domestic sector consumes less or more than it produces", is one of the components used to measure expenditure GDP, and is a potential contributor to GDP growth.[31] Yet the December 2013 Economic and Fiscal outlook reduced the contribution to forecast GDP growth expected from net trade when compared with the March 2013 forecast.[32] On the OBR's forecast for net trade, Mr Chote told us that:

> If you look at it overall in terms of the net trade contribution, which is not just emerging economies, basically we have very little addition to GDP growth from net trade over the course of the five years of the recovery.[33]

He explained that:

> There is a short-term and a medium-term story there. We have had weaker data on exports recently and that has led us to be more cautious in the near term about that. There has been some rewriting of history again in terms of the statistics. I think last

30 Office for National Statistics, Balance of Payments, Q3 2013, 20 December 2013, pp1-2

31 Office for Budget Responsibility, Forecasting the economy, Briefing paper No. 3, October 2011 p32, para 3.86

32 Office for Budget Responsibility, Economic and Fiscal Outlook, March 2013, Cm 8573, p53, Table 3.3; Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 8748, December 2013, p55, Table 3.3

33 Q40

> time we were here we would probably have been talking about the fact that one of the puzzles was that UK market share had deteriorated by more than one would have anticipated given what had been going on with sterling and laying quite a lot of that at the door of financial services exports, which seemed to have been considerably weaker. The data has now been rewritten on that. The financial services export data has been revised up. That does not appear to be so much of a story. The market share figures do not look at puzzling as they did. Looking further out into the medium term, it is the lowering of global growth and global trade forecasts generally that has led us to take a more cautious view of the contributions that net exports can be making in the future. If you look at our aggregate GDP forecasts, we have nudged down 2015, 2016 and 2017 by 0.1 points each again. Not a large number obviously, but it is basically that judgment on the weakness of UK exports markets over that horizon that has led us to do that.[34]

Dr Carney, Governor of the Bank of England, provided the following view of the external environment, and when it would provide support to UK GDP:

> It is a sorry history. For the last five years, whether it is the OECD, the IMF, the Bank of England or indeed the Bank of Canada, where I was previously, about this time every year we were capitulating on our forecasts of global growth and having forecasts where there would be a modest improvement in global growth the following year. This year is no exception, global growth coming in around 3 per cent. The Bank's expectation is global growth will pick up to about 3.5 per cent in 2014; the IMF would be slightly stronger, about 3.75 per cent; the OECD, I think, somewhere around there.
>
> The question is, why would it be different this time, and will we see that actual benefit? Importantly, the reduction of some of the tail risks in Europe help reduce some of the downside risk to that global forecast. The very large swing in the fiscal impulse in the United States from very large drag to less of a drag in the US helps us, as does the improvement in balance sheets in the financial system in the US. The UK helps. As an example, if you improve your financial system, you get much more traction in terms of stimulus. Consumer balance sheets have improved. We have seen the dynamic here.
>
> The downside risks to that improved forecast relate still somewhat to the eurozone, where there is tough execution around a series of structural reforms, and secondly, across a range of emerging markets, where they are going through an adjustment at present to rebalance growth. On that last point, if I may, we have taken that into account and we have substantially marked down the prospects for emerging markets into 2014 such that, in effect, about 70 per cent of the improvement in global growth

34 Q40

> is being driven by the improvement in the core of the advanced economies, which is different than any other time in the recent past.[35]

Business investment

13. Given the forecast lack of a contribution to GDP growth from net trade, business investment is another potential source of GDP growth. Yet growth in business investment has been far weaker than forecast by the OBR even as recently as March 2013. Its forecast for business investment growth in 2013 fell from 1.9 percent in March to -5.5 percent in December.[36] Mr Chote provided the following explanation:

> In terms of thinking why it is that business investment has been weaker than we anticipated you would probably want to point to, first of all, uncertainty about future demand.
>
> The second possibility is that the weakness of profitability means that there is a lack of internal finance for those firms that are reliant on internal finance and also weak productivity implies and the weakness of profits implies weak expected profitability and, therefore, firms thinking, "Is it worth me undertaking an investment programme on that basis?" If we were to look at the three reasons why you have had, over the period since the June 2010, weaker outturns than we anticipated, those are probably the ones that you would point at.
>
> More recently, if you look at page 71[of the Economic and Fiscal Outlook] what is striking is that, since the budget, the ONS has changed the methodology for estimating business investment and we now have a picture that is much more volatile with a steeper fall and a lower average rate of business investment since the recession. We have a business investment deflator, the measure of inflation in that sector, which is now very volatile by historic standards and by the standards of other statistical series for that in other countries.[37]

Brian Hillard, Chief UK Economist, Société Générale was, however, optimistic about a growth of business investment:

> I am reasonably confident it will recover within the next year or two. I think it is surprising that we have such a disconnect between fairly positive business surveys and the weak official data and the Governor of the Bank of England has highlighted that. It is not just a UK issue. It is something that is general to the industrialised economies. We have had a cash-rich corporate sector that I think has been restrained by lack of visibility and demand and I think the conditions are falling in place for that to improve. Domestically certainly we are getting this increase in consumption from whatever source, but internationally we are getting some reduction in the

35 Oral evidence to the Treasury Committee, Bank of England November 2013 Inflation Report, HC 825, Tuesday 26 November 2013, Q62

36 Office for Budget Responsibility, Economic and Fiscal Outlook, March 2013, Cm 8573, March 2013, p9, Table 1.1; Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 8748, December 2013, p10, Table 1.1

37 Q29

> uncertainty in the Eurozone, which I think is a very important backdrop for an improvement. One can't be precise on the timing, but I think the conditions are in place for investment to pick up. I would not suddenly say they are going to leap up within the next six or nine months, but they should be recovering.[38]

When asked what he would do to deliver business investment, the Chancellor told us that:

> I would say above all we can provide a backdrop of economic stability and certainty and solidity to our economic programme. That is what we are doing by having a plan, working through that plan and providing people with the confidence that Britain has a grip on its problems in the public finances and that we are providing a competitive environment in which we can do business with the rest of the world.[39]

14. In February 2014, following the conclusion of our hearings, the ONS released revisions to business investment data since Q1 2013. These revisions, in conjunction with the latest estimate of business investment growth of 2.4% in Q4 2013, show that business investment is estimated to have grown for the last four quarters, from Q1 2013 to Q4 2013.[40]

Productivity

15. Employment has remained stronger than expected given the fall in output since 2008, reflecting a more flexible labour market than many continental EU countries. As noted in NIESR's *Economic Review*, "from the viewpoint of the undesirable nature of unemployment, the increases in employment and consequent decreases in the numbers unemployed are to be welcomed".[41] However, it also means that productivity has declined. This is important, as the NIESR *Economic Review* emphasises that "productivity growth is the key to the evolution of the standard of living of a population in the long run. Low or zero productivity growth limits the growth of real per capita incomes".[42] The OBR noted that:

> Ultimately, productivity-driven growth in real earnings is necessary to sustain the recovery and raise living standards. We therefore expect quarterly GDP growth to slow into 2014, gradually strengthening thereafter as productivity picks up and real earnings growth provides the foundation for a stronger and more sustained upswing. This recovery in productivity growth is perhaps the most important judgement in our economy forecast.[43]

This point was also emphasised to us by the Chancellor, who argued that:

38 Q17

39 Q197

40 ONS, Business Investment, Q4 2013 Provisional Results, Released: 26 February 2014, Table G2

41 National Institute of Economic and Social Research, National Institute Economic Review No. 227, February 2014, pF44

42 National Institute of Economic and Social Research, National Institute Economic Review No. 227, February 2014, pF44

43 Office for Budget Responsibility, Economic and Fiscal Outlook, Cm8748, December 2013, p9, para 1.19

> I think it [the productivity puzzle] remains absolutely an issue of concern. Indeed, I flagged it up in my Autumn Statement speech. Productivity is too low. It is a clear cause for concern in that sense, but the better news is that the OBR forecast that productivity will pick up. They make the observation that, ultimately, a sustainable recovery and a sustainable increase in people's living standards depends on that happening.[44]

16. Charlie Bean, Deputy Governor for Monetary Policy at the Bank of England, told us that one main area of uncertainty was why productivity had been so weak in recent years:

> Certainly, the key issue that faces the economy is how much spare capacity there is. Spare capacity comes in various guises. There is spare capacity in the labour market, which we have been talking about, unemployment, workers who may be part-time rather than full-time, as they would prefer. There may also be spare capacity within companies that they could run at a high level of utilisation. The big unknown that we are faced with, and this ties into the design of the policy guidance, is why productivity growth has been as weak as it has been over the past five years. If you just compare the level of productivity now with the naive extrapolation of the pre-crisis trend, it is about 15 per cent below that. I am not going to suggest we can get back to that 15 per cent trend, but we can probably get some of the way back there.[45]

He provided the following potential explanations of why productivity may have been weak so far:

> There are lots of different hypotheses for why productivity has been weak. Some of these imply that as demand picks up, so you will see productivity analogously responding. There are others that suggest that that productivity may have been permanently lost or pretty persistently lost. That would be particularly the case to the extent that it is associated with weak past investment in the past, workers not having the opportunity to learn by doing because the activity was weak, and to the extent that capital has been misallocated as a result of the problems in the banking system.
>
> We, and many other people, have been trying to get to the bottom of the relative importance of the various causes, but the honest answer is that we do not really know how much productivity will come back as growth proceeds.[46]

The Chancellor provided the following explanation as to why productivity was weak:

> I think we are clear that it is a combination of the impairment of the banking system. That is the primary reason and I think there is an interesting argument, which we

44 Q175

45 Oral evidence to the Treasury Committee, Bank of England November 2013 Inflation Report, HC 825, Tuesday 26 November 2013, Q42

46 Oral evidence to the Treasury Committee, Bank of England November 2013 Inflation Report, HC 825, Tuesday 26 November 2013, Q42

> would give some credence to, about the allocation of resources within an impaired banking system.[47]

The Office for Budget Responsibility's 2012 Forecast Evaluation Report also noted other potential explanations for the productivity puzzle, including undermeasurement of real GDP or capital mismatch, where resources are not reallocated from so-called 'zombie firms' to firms with potentially higher rates of return.[48]

17. Looking forward, the Governor of the Bank of England gave us the following reasons for a potential increase in productivity in the future:

> The first element is just that you have businesses that have slack, and we can think of it in two simple metrics. They are economies of scale and production. They are not producing at optimal scale. The more demand there is, the more they can produce at optimal scale. That is the first element.
>
> The second element is learning by doing. It is a very fundamental point, but the more you produce, the better you get at things, and you end up […] having people move from firms within industries that bring knowledge from best performers to less-good performers, and that improves overall productivity. It is that dynamic first. That is one.
>
> The second dynamic […] is the improvement in the capital labour ratio, the reigniting of business investment. All surveys and other indications suggest that we are close to that point, and in fact, in our forecast, when you go into 2014, consistent with that forecast is really a handover towards business investment and a pickup in business investment.
>
> The third point is a point that Mr Bean emphasised, which was related to the recycling of capital in the economy, so it is poor-performing firms exiting, but very importantly new firms starting up at the same time, so the birth and death of firms. We will look to those types of figures as well to get a sense of whether productivity is coming back.[49]

The Chancellor provided the following argument on the future of productivity growth:

> I do not accept the argument that is made in the United States primarily, but you see spilling over here, that there is some great secular stagnation taking place in the west, that we cannot be more productive or that we cannot provide better living standards for our populations […].[50]

47 Q176

48 Office for Budget Responsibility, Forecast Evaluation Report, October 2012 ,pp39-40

49 Oral evidence to the Treasury Committee, Bank of England November 2013 Inflation Report, HC 825, Tuesday 26 November 2013, Q60

50 Q176

18. **Recent data revisions suggest that GDP has been growing by more than previously thought, and business surveys also suggest that the recovery is taking root. That the recovery is, at the moment, consumer-led, is not surprising. As the Governor of the Bank of England has noted, "recoveries are very seldom, in this country or other countries, led by business investment". However, a broad based improvement in the long run performance of the economy will be required if the recovery is to lead to a long period of trend growth. As we have previously recommended, a greater focus on supply side reform will be required.**

3 The public finances

The fiscal targets

19. The Government's fiscal mandate requires it to have as its objective a balanced cyclically-adjusted current budget by end of the rolling, five-year forecast period. Supplementing this mandate is a target for public sector net debt (PSND) as a percentage of GDP to be falling in 2015/16. Both of these targets are laid down in the Charter for Budget Responsibility, which "sets out the Government's commitment to managing fiscal policy in accordance with clear objectives and targets".[51] In the Economic and Fiscal Outlook (EFO) report accompanying each Budget and Autumn Statement, the OBR forecasts the likelihood of the Government's meeting these targets.

Performance against the fiscal mandate

20. The cyclically-adjusted current budget (CACB) is defined by the OBR as "the amount the Government borrows to finance non-investment spending, adjusted for the state of the economy".[52] The Government's borrowing requirements for non-investment spending would generally be expected to be higher during periods in the economic cycle when the economy was operating below potential. Similarly, these borrowing requirements would be expected to be lower when the economy was operating above potential. The CACB is sometimes known as the 'structural current deficit', since it attempts to strip out the effect of the economic cycle to provide an estimate of the underlying or 'structural' level of borrowing.

21. At the time of Autumn Statement 2013, the OBR forecast that there was a "roughly 80 per cent chance" of the Government balancing the CACB and meeting its fiscal mandate in 2018/19, the final year of the five-year forecast period.[53] This marked an improvement in the Government's performance against the mandate since Budget 2013, when the OBR's judgement had projected a "roughly 70 per cent chance of achieving the fiscal mandate".[54] Table 2 highlights the changes over time in the OBR's forecast of the CACB.

51 HM Treasury, *Charter for Budget Responsibility*, April 2011, pp 5,7

52 Office for Budget Responsibility, *Economic and Fiscal Outlook*, Cm 8748, December 2013, p7, para 1.11

53 Office for Budget Responsibility, December 2013 Economic and Fiscal Outlook Briefing, p9

54 Office for Budget Responsibility, March 2013 Economic and Fiscal Outlook Briefing, p9

Table 2: OBR projections of surplus on the CACB as a percentage of GDP

OBR Report date	Forecast year								
	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Jun-10	-4.8	-3.2	-1.9	-0.7	0.3	0.8			
Nov-10	-4.7	-3.3	-1.8	-0.5	0.5	0.9			
Mar-11	-4.6	-3.2	-2.0	-0.6	0.4	0.8			
Nov-11	**-4.5**	-4.6	-3.9	-2.7	-1.6	-0.6	0.5		
Mar-12	**-4.4**	-4.6	-4.2	-2.7	-1.5	-0.7	0.5		
Dec-12		**-4.3**	-3.6	-2.2	-1.4	-0.8	0.4	0.9	
Mar-13		**-4.2**	-4.0	-2.8	-1.7	-1.2	0.1	0.8	
Dec-13			**-3.6**	-2.9	-2.0	-1.4	-0.2	0.7	1.6

Shaded cells = figures not provided. Bold figures are outturns; otherwise figures are forecasts.

Source: Office for Budget Responsibility, Economic and Fiscal Outlook report, June 2010; Office for Budget Responsibility, Economic and Fiscal Outlook report, November 2010; Office for Budget Responsibility, Economic and Fiscal Outlook report, March 2011; Office for Budget Responsibility, Economic and Fiscal Outlook report, November 2011; Office for Budget Responsibility, Economic and Fiscal Outlook report, March 2012; Office for Budget Responsibility, Economic and Fiscal Outlook report, December 2012; Office for Budget Responsibility, Economic and Fiscal Outlook report, March 2013; and Office for Budget Responsibility, Economic and Fiscal Outlook report, December 2013

22. The March 2013 forecast took 2017/18 as the target year, however, since at the time of the Budget this was the final year in the forecast horizon. Examining the projected surplus on the CACB for each individual year of the forecast period, the OBR projected no improvement relative to its Budget 2013 forecast. In contrast, projections for the surplus on the current budget without cyclical adjustment increased in each year of the December forecast relative to March, as shown in Table 3.

Table 3: OBR projections of surplus on the current budget as a percentage of GDP

OBR Report date	Forecast year								
	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Mar-13		**-6.0**	-6.0	-5.2	-4.3	-3.5	-1.9	-0.9	
Dec-13			**-5.5**	-4.5	-3.3	-2.5	-1.1	0.2	1.4

Shaded cells = figures not provided. Bold figures are outturns; otherwise figures are forecasts.

Source: Office for Budget Responsibility, Economic and Fiscal Outlook report, March 2013; and Office for Budget Responsibility, Economic and Fiscal Outlook report, December 2013

23. The fact that the projected surplus on the current budget increased while the balance on the CACB showed no improvement mirrored the OBR's judgement that "the upward revision to our economic growth forecast since March is cyclical rather than structural".[55] Robert Chote told us:

> we have revised down the deficit, the headline public sector net borrowing in each year going forward in the forecast. Our judgment is that that improvement is primarily cyclical rather than structural. It reflects the fact that we believe that the

55 Office for Budget Responsibility, *Economic and Fiscal Outlook*, Cm 8748, December 2013, p6, para 1.6

> surprisingly high GDP growth over this year is eating into spare capacity, rather than suggesting that at one level of the economy there is more growth potential, [...]. The other changes to what is left, the structural deficit, are relatively modest year by year [...]. The key point is that the deficit is lower, but we are judging that the structural deficit is not significantly lower than we thought in March.[56]

So in the OBR's view, the recent UK economic recovery has been beneficial to the current public finances, having boosted income from taxation and lowered the Government's borrowing requirements. But the recovery has come from economic activity beginning to make its way back to potential—a narrowing of the output gap—rather than any increase in the potential output of the economy.

24. As we noted in our report on Budget 2013, the measurement of the output gap is subject to considerable uncertainty. We concluded:

> The output gap is important to the formulation of monetary and fiscal policy. It is used by the Office for Budget Responsibility when determining the Government's adherence to its fiscal mandate. At the best of times the output gap is inherently hard to measure. The existence of the productivity puzzle makes its estimation even more difficult. A number of possible explanations for the puzzle have been suggested. However, there is currently no agreement about an explanation. It is likely that estimates of the output gap will remain particularly uncertain in the medium term.[57]

Charles Bean, Deputy Governor of the Bank of England (Monetary Policy) also told us that when determining how to "to describe the policy guidance", the output gap was treated with caution by the MPC as "we have no idea how big that is".[58]

25. **The Committee has previously emphasised the considerable uncertainty in the measurement of the output gap and therefore the limit to its usefulness. The OBR's projection of the cyclically-adjusted current budget, which relies upon a forecast of the output gap, is therefore also highly uncertain. Despite these uncertainties, it nevertheless appears that a significant structural deficit has been the inheritance of the last decade, emphasising the need for further fiscal adjustment. Closing the structural deficit will require an improvement in economic performance.**

Performance against supplementary debt target

26. The OBR noted in its December 2013 EFO that the Government was "still on course to miss its supplementary target" for PSND to be falling as a percentage of GDP in 2015/16.[59]

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56 Q63

57 Treasury Committee, Ninth Report of Session 2012-13, *Budget 2013*, HC 1063, para 54

58 Oral evidence to the Treasury Committee, Bank of England November 2013 Inflation Report, HC 825, Tuesday 26 November 2013, Q44

59 Office for Budget Responsibility, *Economic and Fiscal Outlook*, Cm 8748, p165, para 5.11

The OBR forecast that PSND would rise by 1.7 percent of GDP in 2015/16, and fall by a "statistically and fiscally insignificant margin" in 2016/17.[60]

27. The Government has been forecast to miss its supplementary target since the OBR's forecasts at the time of the 2012 Autumn Statement, owing to what it described as "cyclical" drag on the UK economy.[61] At that point, the Government said:

> It is neither necessary nor justified to undertake additional consolidation in the short term in response to the cyclical deterioration in the public finances. It would also constrain the operation of the automatic stabilisers, limiting their ability to support the economy. As a result, the OBR's assessment is that public sector net debt as a percentage of GDP will be falling in 2016–17, a year later than set out in the supplementary debt target.[62]

While choosing not to undertake additional consolidation in order to meet the target, however, the Government did not go as far as scrapping it:

> At this time of rising debt, the Government will restore debt to a sustainable, downward path and will retain the existing supplementary debt target. As set out in the June Budget 2010, the Government will set a new target once the exceptional rise in debt has been addressed.[63]

28. In response, the Treasury Committee, in its report on Autumn Statement 2012, noted that the credibility of the target could be in doubt:

> The possible failure to meet the supplementary target raises the question of the continuing credibility of that target. Successive governments have committed themselves to, but then failed to meet, their fiscal targets. For a fiscal target to be credible, it must be durable, and therefore not subject to frequent revision as circumstances change. It must also be capable of accommodating conditions different from those at the time the target was first formulated.

The Committee felt, however, that the target could retain its value, despite the projection that it would be missed:

> It is not the case, though, that a target is valuable only so long as it is met. A target can remain credible, and so constrain a government's choices, even if it is not being met, so long as the political commitment that created it continues to inform policy decisions.[64]

29. In its subsequent report on Budget 2013, the Treasury Committee expressed agreement with the Government's decision to publish a new fiscal framework "only when the public

60 Office for Budget Responsibility, *Economic and Fiscal Outlook*, Cm 8748, p165, para 5.11

61 HM Treasury, Autumn Statement 2012, Cm 8480, December 2012, p30, para 1.64

62 HM Treasury, Autumn Statement 2012, Cm 8480, December 2012, p30, para 1.65

63 HM Treasury, Autumn Statement 2012, Cm 8480 December 2012, p31, para 1.68

64 Treasury Committee, Seventh Report of Session 2012-13, *Autumn Statement 2012*, HC 818-I, para 48

finances are returning to a more stable position".[65] However, as the Treasury Committee noted in its report on Autumn Statement 2012, the timetable for the review of the target—to take place "once the exceptional rise in debt has been addressed"— was "vague".[66]

A new Charter for Budget Responsibility

30. In Autumn Statement 2013, the Government announced a review of the Charter for Budget Responsibility, scheduled to take place in 2014. This review, the Government noted, would examine changes to the fiscal framework:

> The Government will now begin a review of the current framework, reporting next year.
>
> The review will consider several questions, including:
>
> - What is the appropriate time horizon for the fiscal mandate once the structural current deficit is closer to balance?
> - How could fiscal credibility be further enhanced by a stronger Parliamentary commitment to the path of consolidation in 2016/17 and 2017/18?[67]

The updated Charter would also be used to provide the Parliamentary framework for the Government's welfare reduction plans:

> The government will establish [the] framework for the welfare cap as part of the Charter for Budget Responsibility [...]. The Charter will specify:
>
> - the requirement for a cap
> - the expectation on the government to bring forward a vote in the House of Commons when setting the level of the cap, if it wants to change the level of the cap, and if it breaches the cap
> - the role of the OBR in assessing the government's performance against the cap.[68]

31. As set out in the Budget Responsibility and National Audit Act 2011, any modified Charter for Budget Responsibility would need to be approved by a resolution of the House of Commons before coming into effect.[69] In his Autumn Statement to the House on 5 December 2013, the Chancellor confirmed that the Government would ask Parliament to

65 Treasury Committee, Ninth Report of Session 2012-13, *Budget 2013*, HC 1063, para 62

66 Treasury Committee, Seventh Report of Session 2012-13, *Autumn Statement 2012*, HC 818-I, para 49

67 HM Treasury, Autumn Statement 2013, Cm 8747, December 2013, p39, para 1.136

68 HM Treasury, Autumn Statement 2013, Cm 8747, December 2013, p39, para 1.117

69 Budget Responsibility and National Audit Act 2011, Section 1

support the new Charter, which would be laid before it alongside the Autumn Statement 2014.[70]

32. The Treasury Committee has in the past recommended that any amendments to the fiscal framework also be subject to full public consultation. In its report on Autumn Statement 2012, the Committee said:

> When the Government does decide to create a new fiscal framework, it should do so only after full public consultation. The Committee will return to this issue.[71]

And in its report on Budget 2013, the Committee reiterated:

> We agree with the Government that a new fiscal framework should be published only when the public finances are returning to a more stable position. Public consultation should then take place on the basis of those proposals in an environment that does not endanger market credibility.[72]

33. **It is not yet clear what the outcome of the Government's review of the Charter for Budget Responsibility will be. It is reasonable to suppose that it may contain amendments to the fiscal mandate. This Committee has previously recommended that any new fiscal framework should be subject to full public consultation. The requirement for the updated Charter for Budget Responsibility, including any amended fiscal framework, to be approved by the House of Commons, falls some way short of this proposal. The Government should consult on any proposed changes to the fiscal framework as part of its review of the Charter for Budget Responsibility. Effective public consultation will improve the prospects of creating a framework for fiscal policy that will be more stable and resilient than those used in the past.**

The future path of public spending

Ring-fencing

34. In Autumn Statement 2013, the Government confirmed that it would continue its policy of 'ring-fencing' certain departmental budgets. Expenditure on Health, schools and Official Development Assistance (ODA) would "be protected in line with the policy set out at Spending Round 2013". Other resource departmental expenditure limits (RDEL) would share additional cuts of £1.1bn in 2014/15 and £1bn in 2015/16.[73] Local government spending, HMRC and the Single Intelligence Account were also exempted from these new spending reductions, although the Chancellor told the Treasury Committee that:

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70 HC Deb (2013-14), 5 December 2013, Col 1104 [Commons Chamber]

71 Treasury Committee, Seventh Report of Session 2012-13, *Autumn Statement 2012*, HC 818-I, para 49

72 Treasury Committee, Ninth Report of Session 2012-13, *Budget 2013*, HC 1063, para 62

73 HM Treasury, *Autumn Statement 2013*, Cm 8747, December 2013, p81, para 2.7

> I would not say that those are ring-fenced. Those were individual decisions that I took this year.[74]

35. Paul Johnson, Director of the Institute for Fiscal Studies (IFS) pointed out in addition the ring-fencing of pension benefits:

> You have pensioner benefits that appear to be largely ring-fenced there, north of £100 billion a year of ring-fencing.[75]

The Government outlined explicitly the protection of pensions following the Committee's evidence sessions, confirming its commitment to increase the size of the state pension by at least 2.5 percent per year in the next Parliament.[76]

36. The Treasury Committee has expressed its concern about ring-fencing. For example, in its report on Budget 2013, we said:

> As the Committee has previously highlighted, the complete protection of ring-fenced departmental budgets will become more difficult for the Government with each successive year of tightening. Ring-fencing carries political attractions for any government, but it threatens to reduce scrutiny of ring-fenced spending, it can lead to waste or worse and it can distort the balance of spending as a whole.[77]

37. One of the consequences of ring-fencing is sharply to alter the overall composition of public spending. Paul Johnson told us:

> By keeping pensions, health and schools, which are three of the very biggest chunks, entirely unaffected while taking a lot out of the rest, the effect of ring-fencing is to dramatically change the shape of what Government is doing.[78]

Table 4: Changing composition of DEL

	Share of DEL (per cent)			
Financial year	**NHS**	**Schools**	**ODA**	**Other DEL**
2010–11	26.4	9.8	2.2	61.6
2011–12	27.9	10.4	2.3	59.4
2012–13	29.2	10.9	2.4	57.5
2013–14	29.7	10.8	3.0	56.5
2014–15	30.3	11.0	3.1	55.6
2015–16	31.0	11.2	3.3	54.5
2016–17	32.0	11.6	3.5	52.9
2017–18	33.6	12.2	3.8	50.4
2018–19	34.6	12.5	4.0	48.9

Note: The DEL total is consistent with that used in the 2014 IFS Green Budget, and has been adjusted for various transfers between DEL and AME to derive a consistent series over time.

Source: IFS written evidence, PESA 2013, Autumn Statement 2013, Spending Review 2013, DfID statistics on Overseas Development Assistance spending.

74 Q146

75 Q237

76 "*David Cameron pledges to 'protect' the state pension*", BBC News, 5 January 2014

77 Treasury Committee, Ninth Report of Session 2012-13, *Budget 2013*, HC 1063, para 137

78 Q237

The IFS noted in their written evidence that:

> These protected areas, particularly the NHS and schools, are taking up an increasing share of a diminishing pool of resources. As a matter of arithmetic continuing to ring fence them will place increasing pressure on other budgets.[79]

The IFS provided further evidence, see Table 4, showing the effect on the non-ring-fenced DELs if the current ring-fences were maintained, and the Government's planned levels of total public spending and current policy on Annually Managed Expenditure was followed.[80] The IFS told us however that "The Chancellor has mooted the possibility of an additional £12 billion of cuts to social security spending, which could be used to ease the cuts to DEL." Table 5 shows the effect on the unprotected DELs if the £12 billion reduction in social security spending were used to reduce the cuts to DELs, while maintaining the ring-fence.

Table 5: Changing composition of DEL, assuming cuts to spending on unprotected areas in 2018–19 reduced by £12 billion

Financial year	Share of DEL (per cent)			
	NHS	Schools	ODA	Other DEL
2010–11	26.4	9.8	2.2	61.6
2018–19	33.3	12.1	3.8	50.8

Note: The DEL total assumes £12 billion is cut from social security spending by 2018–19 and allocated to unprotected departments.

Source: IFS written evidence, PESA 2013, Autumn Statement 2013, Spending Review 2013, DfID statistics on Overseas Development Assistance spending .

38. In 2012, the British Social Attitudes survey asked people what would be their "highest priority for extra [government] spending" against a list of possible options: 41.9% said health, 30.0% education and 0.5% overseas aid. When asked for their next preference, 31.5% said education, 29.4% health and 0.5% overseas aid.[81] The Chancellor explained that the Government's aim in ring-fencing certain departmental budgets was to reflect the public preference:

> I think what it is a reflection of is where the public wants their money spent. It is the public's money, not my money or, dare I say it, Parliament's money. It is the public's money and the public have made it very clear that their priorities are things like the national health service. [...] It is up to all of us, which every party we represent, to seek to reflect and represent the aspirations of the British people and I think the decisions we have made on what budgets get a relative priority are representative of that.[82]

79 Institute for Fiscal Studies, written evidence

80 Institute for Fiscal Studies, written evidence

81 NatCen Social Research, British Social Attitudes 30, British Social Attitudes 2012 Face-to-face questionnaire, Qq299-300

82 Q149

39. This assessment was echoed in part by Paul Johnson, who told the Committee:

> One observes that the protection for health is politically popular and has been over a long period and that the demands on the health service are growing, so there is a remarkable degree of political bipartisanship around some of this. [83]

Mr Johnson also noted, however, that there was inadequate public discussion about the trade-offs involved in choosing where to focus public spending:

> What is much harder to get a handle on is the extent to which people recognise the long-run effects in terms of reductions in things like infrastructure spending, but also in a lot of the areas of local government and justice and the environment and so on. I do not think we do have an adequate political discussion about the trade-offs. Trade-offs are a difficult thing to have a public discussion about, but the trade-offs in the long run clearly are very substantial.[84]

Welfare

40. The Autumn Statement 2013 confirmed that, in line with previous policy for fiscal consolidation, the Government's Total Managed Expenditure (TME) would continue to fall in 2016/17 and 2017/18 at the same real rate as over the current Parliament, bringing its level to 38.4 per cent of UK GDP by 2018/19.[85] TME includes both expenditure on public services and administration, and Annually Managed Expenditure (AME), which largely comprises social security and debt interest.

41. In its December 2013 EFO, the OBR forecast that, on the basis of current policy, "over the nine years from 2009/10 [...] government consumption of goods and services— a rough proxy for day-to-day spending on public services and administration— [will have fallen] to its smallest share of national income at least since 1948".[86] The Chancellor told us, however, that this projection relied on an "erroneous judgement about what the political system would do":

> I think they are perfectly right that on the current plans, that is what it shows, but I think the next Government will want to undertake further reductions in the welfare budget and further welfare savings. If you undertake further welfare savings, then you do not reach that 1948 number.[87]

42. While he did not place specific numbers on the Government's plans, the Chancellor confirmed that "many billions of pounds of welfare savings are going to be required", and that:[88]

83 Q243

84 Q 243

85 HM Treasury, Autumn Statement 2013, Cm 8747, December 2013, pp80-81, para 2.5 and Table 2.3

86 Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 8748, December 2013, p7, para 1.10

87 Q182

88 Q219

> My view is that welfare expenditure cannot be excluded from the difficult decisions that need to be made. If you want to maintain the same pace of reduction in Government spending that we have had over this Parliament rather than accelerating it, then you are going to have to find billions of pounds of welfare savings and I think that is what this country needs to do, personally.[89]

43. The IFS estimated that avoiding an acceleration in public service spending cuts would "require cuts in welfare (or other AME) spending of a further £12 billion a year by 2018–19".[90] Describing the effect of such reductions in welfare spending, Paul Johnson said:

> By not indexing for inflation those benefits over a period of years, you could get that kind of money if you get a couple of per cent a year over a Parliament. It is that sort of scale, I guess. It is saying, "We are going to stop indexing these benefits for five years".[91]

44. Following the Committee's evidence sessions, in a speech on 6 January 2014, the Chancellor appeared to confirm the IFS figures, noting that "on the Treasury's current forecasts, £12 billion of further welfare cuts are needed in the first two years of next Parliament [...] to reduce the deficit without even faster cuts to government departments, or big tax rises on people".[92]

Conclusions

45. **Ring-fencing, by definition, requires that the balance of public expenditure restraint and cuts be borne in the rest of public expenditure. Each successive year of public expenditure restraint results in an increase in ring-fenced spending as a proportion of the total. The smaller non-ring-fenced areas in turn have to bear a higher proportion of any savings in subsequent years. The IFS has shown that non-ring-fenced expenditure may fall from 61.6 per cent in 2010–11 to around 50 per cent in 2018–19 of total Departmental Expenditure Limits. Ring fencing also reduces the discipline on spending in these areas: the rigour of negotiations between the department and the Treasury on allocations will be weakened, since it is known in advance by both sides that this spending is protected.**

46. **The Chancellor says that the ring-fencing of health, schools and overseas aid budgets reflects public preferences. Protection of health and education spending, but not overseas aid, appears to reflect public preferences.**

47. **The Government should do what it can to ensure sufficiently informed public debate on the trade-offs inherent in ring-fencing and the allocation of spending cuts.**

89 Q186

90 Institute for Fiscal Studies, Paul Johnson, Introductory remarks to IFS Autumn Statement 2013 briefing, 6 December 2013, pp 2-3

91 Q241

92 Speech by the Chancellor of the Exchequer, Rt Hon George Osborne MP, Sertec Group's Head Office in Coleshill, 6 January 2014

Such a debate is especially important in a period of transformative spending reductions.

4 Housing

House prices and supply

48. There has been a resurgence in house prices across the UK. Data from the Office for National Statistics show that house prices grew in the twelve months to October 2013 by 5.5 percent, with prices in London growing at 12 percent over the same period.[93] Recent price indices from Nationwide showed a more rapid trend towards the end of the year, with prices rising nationally by 7.1 percent, and by 14.9 percent in London during the whole of 2013.[94] The 2013 Q4 Credit Conditions Survey from the Bank of England also indicates that secured lending conditions have eased recently:

> In the three months to early December, lenders reported that the availability of secured credit to households increased. An increase in availability was reported for borrowers with loan to value (LTV) ratios above 75%, and there was also an increased willingness to lend at LTV ratios above 90%. The expansion in overall availability was driven by market share objectives, higher expectations for house prices and an increased appetite for risk. Consistent with an increased risk appetite, credit scoring criteria were loosened and the proportion of loan applications being approved increased significantly.
>
> Lenders expected the availability of secured credit to significantly increase in 2014 Q1, including for those borrowers with a LTV ratio above 75% and 90%. Many lenders attributed the increased availability at the highest LTV ratios to participation in the Government's Help to Buy Scheme, while some others attributed it to increased competition associated with the Scheme. Consistent with a move into higher LTV lending, lenders expected the average credit quality of new lending to fall over the next quarter.
>
> […]
>
> Lenders reported that demand for secured lending to finance a house purchase increased significantly in Q4, with the net percentage balance rising to its highest level since the survey began. Lenders also reported that demand for secured lending for remortgaging increased significantly in 2013 Q4. Some lenders suggested that the increase in demand was supported by first-time buyer and homemover interest in the Government's Help to Buy Scheme. Competitive pricing and increased promotional activity was also reported to have stimulated demand. Lenders expected little change in demand for secured lending in 2014 Q1.[95]

49. NIESR notes that rising house prices may stimulate consumption:

93 "House Price Index, October 2013," Office for National Statistics, 17 December 2013

94 "Nationwide House Price Index, Q4 2013," Nationwide, 3 January 2014

95 Bank of England, Credit Conditions Survey, 2013 Q4, pp3

> Stronger house price inflation outturns would lead us to lift our forecast for consumer spending growth this year. The consumer spending equation for the UK is based on the estimated equation in Barrell and Davis (2007). NiGEM simulations suggest the rule of thumb that a 10 per cent increase in house prices raises consumption by 1 per cent in the first year.[96]

But rapidly rising house prices also may be a cause for concern. As NIESR notes, "In the short term the housing market presents a challenge for policymakers. Increasingly rapid rates of house price inflation could well be an increasing cause of concern for both the Financial Policy Committee and the [Monetary Policy Committee]".[97] At his appointment hearing in October 2013, the Committee asked Sir Jon Cunliffe, the new Deputy Governor for Financial Stability at the Bank of England, whether he thought a housing bubble was forming in the UK. He said:

> I am not sure I would agree that we are entering into a housing bubble. I would agree that house prices have risen pretty quickly this year and also that expectations of future house prices have risen, but it is coming from a relatively low base. Compared to some historic measures, housing activity is still not back to levels we saw before the crisis. House prices to income ratios are probably where they were about 10 years ago.
>
> [...]
>
> Is it something that needs to be watched very carefully? Yes. Does the UK have a history of housing booms? Most certainly. Is it something that would need to be dealt with if it posed a risk to financial stability? Yes, but I think it is too early to say whether we are entering into a bubble.[98]

For his appointment hearing, the Governor of the Bank of England noted that:

> Certain asset prices, but more importantly measures of credit growth, may also provide a useful signal about potential risks to price stability beyond the usual inflation target horizon. Indeed, experience has shown that imbalances fuelled by a credit boom, which may manifest themselves in asset-price movements, pose the greatest medium-term risk to the economy, because of the powerful deleveraging process they induce when they unwind.[99]

50. Whilst house prices have risen rapidly over the past year, the Committee heard evidence to suggest that such price rises may continue. In its December 2013 Economic and Fiscal Outlook, the OBR forecast national house price increases of 5.2 percent, 7.2

96 National Institute of Economic and Social Research, National Institute Economic Review No. 227, February 2014, pF50; Barrell, R. and Davis, E.P. (2007), 'Financial liberalisation, consumption and wealth effects in 7 OECD economies', Scottish Journal of Political Economy, 54, 2, pp. 254–67.

97 National Institute of Economic and Social Research, National Institute Economic Review No. 227, February 2014, pF51

98 Oral Evidence by Sir Jon Cunliffe to the Treasury Committee, *Appointment of Sir Jon Cunliffe as deputy governor of the Bank of England*, 14 October 2013, Q25

99 Treasury Committee, Eighth Report of Session 2012-13, *Appointment of Dr Mark Carney as Governor of the Bank of England*, HC 944, Ev39

percent and 4.8 percent in 2014, 2015 and 2016 respectively.[100] Robert Chote, Chairman of the Office for Budget Responsibility, explained that the OBR's view was driven by market fundamentals—particularly a lack of supply—and did not indicate a bubble:

> There is an issue here about whether house prices are rising and houses are expensive in some people's view for fundamental reasons, that we have more demand and relatively inelastic supply, rather than what you might think of a classic bubble, which is, leaving those fundamentals aside, people see prices rising and want to exploit the future rise in prices that they expect. That is one reason why I do not think we would use the "bubble" language.
>
> [...]
>
> In terms of policy effects and so on [...] there are a variety of factors that are increasing demand, but we have very inelastic supply. You would indeed need to have a very big increase in house building to make enough of a difference to the stock to be making a great deal of difference on the price side.[101]

Sir Jon Cunliffe also stressed the importance of underlying market fundamentals, noting that "in the end, the issue comes down to a structural imbalance between supply and demand, which we have not managed to tackle."[102]

51. Economists appearing in front of the Committee also broadly agreed that a shortage of supply was one reason for high house prices. Alan Clarke, Director of Fixed Income Strategy at London Scotiabank, believed that supply had contributed to recent house price rises, noting that despite the recent economic downturn, demand for homes had still outstripped supply:

> [...] in the last couple of years we were not building enough homes to keep pace with the growth in household formation. We have migrant workers potentially coming from Bulgaria and Romania and that will only intensify. Demand clearly fluctuates, as it would do. Supply has been lacking [...]. In the deepest recession since the war prices went down, but not nearly as much as they could have done because supply just was not there. There was not the excess supply and maybe that saved us from an even worse downturn, but clearly it did demonstrate we do lack supply."[103]

Mr Hilliard, Chief UK Economist, Société Générale, added that whilst increased demand from policy stimulus would lead to a supply response, the response would likely remain insufficient to prevent sharp house price increases in the near future:

> [...] what we are seeing in the short term is that the stimulus from policy is driving up demand more quickly than supply. That is why we are seeing such a sharp

100 "Economic and Fiscal Outlook", Office for Budget Responsibility, December 2013, p 84, table 3.5

101 Q24

102 Oral Evidence by Sir Jon Cunliffe to the Treasury Committee, *Appointment of Sir Jon Cunliffe as deputy governor of the Bank of England*, 14 October 2013, Q27

103 Q32

> acceleration in house price inflation and I think we should expect that to continue in the short term. It is very uneven. I think we tend to colour our judgment by being seated in London and seeing the very sharp increases in prices here. Some regions are not experiencing price increases at all yet. They will, but it is a demand-led story that is going to bring forward some supply but I am not confident it will bring forward enough supply to level prices out quickly.[104]

The Chancellor also agreed that supply was a problem, noting that "the answer for this country [...] is we need more homes".[105]

52. When questioned on the causes of this undersupply, Mr Clarke noted that planning constraints proved a problem, but also that "we are a small island nation and there is only so many houses you can build on the land that we have".[106] Mr Hillard agreed that planning constraints were a problem, noting that they had been "in place for a long time." However, he disagreed that there was a lack of suitable land to build on in Britain.[106]

53. Paul Smee, Director General of the Council of Mortgage Lenders, explained why the CML was more relaxed about the prospect of a new housing boom. He believed that that constraints in affordability caused by slow rises in real incomes, and the new regulatory regime, would have an impact.[107] Mr Clarke, whilst believing that house price rises would hit "double digits",[108] noted that recent rapid price rises could represent a temporary, short term unwinding of pent-up demand:

> There is an element of pent-up demand of three years and that will get tired legs. I think you have new supply coming on from Help to Buy. It is a slow process. You also have people who may have bought a house at £200,000, the price dropped to £150,000 and they were reluctant to sell at that point and crystallise a loss. Now that house prices are getting back to where they were I think you will see more supply of legacy owners coming back on to the market and maybe giving an automatic stabiliser.[109]

54. **Data from the end of 2013 indicate that national aggregate house prices have recently been growing at a rapid rate. Mortgage availability, and the demand for mortgages, have both increased. The growth in house prices has drawn considerable public attention, particularly regarding whether the activity yet represents a speculative housing bubble. Witnesses explained rising prices by drawing attention to pent-up demand and the limited supply of housing within the UK, and to the likelihood of a limited short-term supply response to rising house prices.**

104 Q33

105 Q164

106 Q33

107 Q299

108 Q109

109 Q117

55. **The danger is that it will be difficult for the Financial Policy Committee to identify when a speculative housing bubble may have begun. Such a bubble, driven by increasing lending to households, would be a risk to the UK economy. As the Governor has told us, "experience has shown that imbalances fuelled by a credit boom, which may manifest themselves in asset-price movements, pose the greatest medium-term risk to the economy, because of the powerful deleveraging process they induce when they unwind." House prices are therefore a class of asset price which requires careful attention by policymakers, given their historic and continuing influence on the UK economy.**

Exiting Help to Buy

56. The Treasury Committee has previously been critical of the Government's Help to Buy: Mortgage Guarantee scheme. In its Report into the 2013 Spending Round, the Committee concluded that the role envisaged by the Chancellor for the FPC was not as strong as it first seemed:

> Following Committee scrutiny it transpires that the so-called "double lock"—whereby we initially understood that the FPC would have a veto over the continuation of the scheme after three years—is not a lock at all. Our understanding is that the government of the day, if it chose to extend the scheme, could do so despite any objections raised by the FPC. The Government should provide more precise information on the operation of the so-called "double lock" and, in particular, re-examine the case for giving the FPC an explicit veto over the continuation of the scheme.[110]

The Committee also concluded that "without a corresponding supply response, the scheme could serve merely to drive up house prices,", as well as expressing concern regarding "the appropriateness of the taxpayer acquiring contingent liabilities" and the possibility of the taxpayer footing the bill for losses. The Committee also expressed concern about potential for political pressure for the scheme to continue.[111]

57. At the time of the Autumn Statement, the Chancellor again described the FPC's assessment of Help to Buy: Mortgage Guarantee at the end of the scheme as a "lock", stating that "the Financial Policy Committee have a lock because the scheme, even if someone wanted to, cannot be extended without their consent." However, when questioned on the ability of the FPC to veto the scheme, the Chancellor clarified that the FPC would act only as advisor, albeit an influential one. He said:

> Ultimately, I think decisions about housing schemes, which after all use the Government's balance sheet, are decisions for Government and for Parliament. We have not handed over the responsibility and the accountability for that to the Bank of

110 "Spending Round 2013," Treasury Committee, Third Report of Session 2013–14, HC 575, 11 September 2013, p 31, para 56

111 "Spending Round 2013," Treasury Committee, Third Report of Session 2013–14, HC 575, 11 September 2013, p 31, para 55

England, but the Bank of England, of course, have a very powerful advisory role and have specific instruments in the housing market space that they can use around capital requirements and the like and mortgage standards. What I would say is, of course, if the FPC were to provide us with advice we would do well to pay attention to it.[112]

58. The Help to Buy: Mortgage Guarantee has a three year life, at the end of which a future government has the option to extend the scheme. At that time, the Government has also undertaken that the Financial Policy Committee will be asked to give its assessment on the impact of the scheme on financial stability.[113] The Help to Buy: Equity Loan schemes also have a three year life from a start date of 1 April 2013.[114] When questioned on the end of Help to Buy, Paul Smee, Director General of the Council for Mortgage Lenders, noted that there was a risk of a 'cliff edge' at the end of the policy:

> I have been talking for some time about the need for a proper exit strategy that avoids this cliff edge, both under the mortgage guarantee and equity loan, which can give rise to unusual activity toward the end of the scheme and then no activity thereafter.[115]

Nigel Terrington, Chairman of the Council for Mortgage Lenders, noted in a speech in November 2013 that the need for scheme exit design was "driven by the experience of previous schemes" and that "careful planning can avoid this mood swing."[116]

59. Mr Smee said that tapering the scheme at its end was one potential solution[117]. He suggested that a method of doing this would be to "increase the cost of accessing the scheme, which would make the source of funds under Help to Buy less attractive to lenders, so they might cease to put loans into the scheme."[118] Mr Smee also warned that any taper should begin "before three years, so that the scheme can close after three years."[119]

60. **The Committee has previously concluded that the Help to Buy: Mortgage Guarantee scheme could produce negative distorting effects on the housing market. Our judgement has not changed.**

61. **In addition to this, the Government's Help to Buy: Mortgage Guarantee scheme may have further distorting effects on the UK housing market when withdrawn. The Treasury should examine the impact of an abrupt end to this scheme, and act in advance to mitigate market distortions before they arise. The Government should**

112 Q22

113 Written Ministerial Statement 'Publication of Help to Buy: mortgage guarantee scheme rules and fee', 8 October 2013

114 "Budget 2013," HM Treasury, March 2013, pp 38-39, paras 1.101-1.102

115 Q278

116 Speech by the CML chairman Nigel Terrington at the CML Mortgage Industry Conference & Exhibition, 6 November 2013

117 Q305

118 Q291

119 Q306

explain now what the exit strategy from Help to Buy: Mortgage Guarantee will be in order better to influence expectations. The Bank of England may need to adjust the timing of its regular annual review of the Help to Buy: Mortgage Guarantee scheme accordingly.

5 Individual measures

Dynamic effects of taxation

62. At the time of the Autumn Statement, the Government published a study into the dynamic effects of taxation. This assessed how tax policy changes might lead to wider economic behavioural changes, for example increased business investment in the case of corporation tax. The Treasury study focused, in particular, on the long run dynamic effects on growth of the Government's corporation tax cut from 28 per cent to 20 per cent.[120] The Treasury's analysis suggests that the tax cut could lead to a 2.5 per cent to 4.5 per cent increase in investment, a 0.6 per cent to 0.8 per cent increase in GDP, and higher wages and increased consumption.[120]

63. The results of the modelling exercise, as with all economic modelling, are subject to some degree of uncertainty. The Treasury's paper states:

> The CGE model is subject to some uncertainty. This is principally around the parameters included, for which sensitivity analysis is carried out. Economic uncertainty, not captured by the model, could also impact on the results in the short term. Nevertheless, the results are broadly consistent with the wider academic literature which finds that reductions in Corporation Tax boost investment leading to higher GDP and partial revenue recovery. [120]

Mr Emmerson of the IFS also emphasised the uncertainties involved:

> Clearly you have to be very careful, because if you change those assumptions, you could get a different answer and the pay-off is over a very long time. It is not like you can do the change and then see a year later whether it has worked out. You have to wait 20 years before you get the full response if the model is correct. Clearly there are risks there and there are a lot of uncertainties.[121]

64. However, given the limitations of the model itself, Mr Emmerson said that the "assumptions they have made certainly do not look unreasonable" and that it was a worthwhile exercise.[122]

65. The Chancellor said that his rationale for asking the Treasury to produce the paper was:

> It is something I had said needed to be done when I was in Opposition and it reflects a debate that is had, I would not just say on the centre right of British politics, but primarily on the centre right, which is that lower taxes can, at least in part, pay for themselves through the additional investment and economic growth they bring.

120 "Analysis of the dynamic effects of Corporation Tax reductions," HM Treasury and HM Revenue and Customs, 5 December 2013, p 3

121 Q254

122 Q254

> [...]
>
> I did want to move the debate and begin a quiet revolution in the way people think about these things and so I started with corporation tax and commissioned this study.[123]

However, the Chancellor was clear that the existing "static scoring" system used by the Office for Budget Responsibility would continue for at least the near future, and stated that the purpose of the paper was purely to add to the existing debate:

> We have a static scorecard and an established system of costing things, and of course now a major innovation in this Parliament, we have an Independent Office for Budget Responsibility that audits those things.
>
> [...]
>
> I would certainly envisage for this Parliament continuing to use the static scoring as the basis of the budgets in Autumn statements, but these studies of individual taxes are what I think helps shift the debate in a positive way.[124]

Mr Chote agreed, stating that "the work they are doing in that area we read with interest and we will look and see how it informs our own", [125] but also making it clear that the OBR had not certified the model and that the outcome of the study had not influenced the OBR's forecasts.[126] Mr Chote also noted that a number of the modelled outcomes of the paper were already taken into account in the OBR's existing "static scoring" system:

> You have outlined a number of the interesting effects there, one of which is the reduction in corporation tax reduces the cost of capital, encourages business investment with a potential knock-on effect on GDP. That is in the forecast. We make adjustments for that effect when we have included corporation tax measures in the past. We have pushed up business investment by, I think, roughly the same proportion, 3 per cent or so, as this paper would suggest.
>
> The paper also points out that you need to look at the impact of profit shifting. Again, our forecasts have made an adjustment for profit shifting, which reduces the direct static cost of the measures. The area where I think this analysis suggests more impact than we would include is the fact that it does more to boost consumer spending than it does to boost investment.
>
> [...]
>
> It is important to bear in mind that this paper is not a comparison between the way we treat these things and an alternative way. Quite a lot of the stuff that they are

123 Q59

124 Q59

125 Q42

126 Q43; Q 46

> highlighting as potential effects are things that we take into account when we are doing our forecast anyway.[127]

66. **The Treasury's analysis of the dynamic effects of the Government's corporation tax cut is subject to great uncertainty. Nonetheless, there is some merit in continuing to study the dynamic effects of policy decisions. It is important to emphasise, however, that the OBR took account of some of the effects of the Government's corporation tax cut discussed in the Treasury's paper in its own forecasts, including the effects on business investment and profit shifting. The OBR has stated that the Treasury's analysis has not affected its official economic forecasts. We will expect the OBR to continue to reach its own independent judgement on the effects of tax changes on the yield.**

UK-Swiss tax co-operation agreement

67. The UK-Swiss tax co-operation agreement became effective on 1 January 2013. The agreement, originally signed in 2011, ensured that deposits of UK residents held in Swiss bank accounts became subject to a one-off payment to clear past unpaid tax liabilities, and a withholding tax on future income and gains.[128]

68. The OBR provided indicative costings for the policy in its December 2012 EFO, putting its likely total yield at £5.3bn from 2012/13 to 2017/18.[129] The Treasury Committee, in its report on Autumn Statement 2012, concluded that:

> the proceeds [of the agreement] may not meet expectations if assumptions about the potential tax liabilities and expected behaviour of those affected prove not to be valid.[130]

69. In its response to the Treasury Committee's report on Budget 2013, the OBR highlighted some of the key uncertainties surrounding its costing of the policy, and confirmed that it would revisit its analysis at the time of the Autumn Statement:

> The key uncertainties for the UK-Swiss tax agreement are the value of UK financial assets in Switzerland and the behavioural response of those individuals with funds in Switzerland. (Indeed, we made a lower estimate of the likely yield than that originally made public by ministers and HMRC because we preferred a lower central forecast for the pool of assets.) We will re-assess the yield from the agreement in our Autumn 2013 forecast [...].[131]

The Treasury Committee said in its report on Budget 2013:

127 Q 42

128 HMRC, '*The Swiss/UK Tax Cooperation Agreement and HM Revenue & Customs (HMRC)*', October 2012

129 Office for Budget Responsibility, Economic and Fiscal Outlook, December 2013, Cm 8748, p114, Box 4.3

130 Treasury Committee, Seventh Report of Session 2012-13, *Autumn Statement 2012*, HC 818-I, para 77

131 Treasury Committee, Second Special Report of Session 2013-14, *Budget 2013: Government and Office for Budget Responsibility Responses to the Committee's Ninth Report of Session 2012-13*, HC 370, p20

> We will monitor closely whether the agreement with Switzerland produces the receipts the OBR has forecast for this financial year.[132]

Table 6: Costing of UK-Swiss Tax Co-operation Agreement

£bn	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	Total
Autumn Statement 2012	0.3	3.1	0.6	0.9	0.2	0.2	5.3
Autumn Statement 2013	0.0	1.1	0.3	0.3	0.1	0.1	1.9
Reduction	0.3	2.0	0.3	0.6	0.1	0.1	3.4

Source: Office for Budget Responsibility Economic and Fiscal Outlook, December 2013

70. When the OBR came to re-assess the likely yield from the UK-Swiss tax agreement in its December 2013 EFO, it reported a reduced projection of £1.9bn over the forecast period.[133] The reasons for this reduction were linked clearly to the uncertainties the OBR pointed out in its March EFO:

> At the time [of the original costing], we stressed the uncertainty of the original costing due to the lack of hard information about the value of UK individuals' financial assets in Switzerland, and how these individuals would respond to the policy. Both receipts data and the July announcement from the Swiss Bankers' Association (SBA) indicate that the yield from the one-off levy (Swiss capital tax) will be significantly lower than estimated in the certified costing. [...]
>
> The lower-than-expected yield is likely to reflect both a smaller initial tax base and a larger behavioural response than was estimated. The smaller tax base is likely to reflect some combination of: fewer assets held by UK individuals in Swiss banks; more of the assets belonging to non-domiciles or people who are already compliant; and the failure of Swiss banks to identify UK individuals holding assets; or circumvention of the deal. The SBA announcement suggested a high number of individuals with non-domicile status. The extent of capital flight to other offshore centres is likely to have been greater than expected. [134]

71. The OBR has previously conceded that there are uncertainties in forecasting income from anti-avoidance measures generally. In its response to the Committee's Budget 2013 report, the OBR noted:

> We agree that the yield from anti-avoidance measures is generally more uncertain than that from other policy measures [...]. Key uncertainties include how much avoidance is currently taking place and the extent to which firms or individuals have opportunities for other avoidance routes. Many avoidance costings allow for attrition, in other words an expectation that revenue from the measure will decline

132 Treasury Committee, Ninth Report of Session 2012-13, *Budget 2013*, HC 1063, para 64

133 Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 8748, December 2013, p115, Box 4.3

134 Office for Budget Responsibility, Economic and Fiscal Outlook, Cm 8748, December 2013, p115, Box 4.3

> over the forecast period as new avoidance routes are discovered. We are working with HMRC to improve the evaluation of anti-avoidance measures. We hope this will help improve future costings, for example the attrition rates adopted.[135]

The OBR added that it is not easy to learn lessons from the success or otherwise of past anti-avoidance measures:

> When we receive costings for anti-avoidance measures, we routinely ask whether there is evidence on the likely yield from similar measures in the past. But unfortunately there is a limit to what can be learned from examining past anti-avoidance measures, as there is always considerable uncertainty regarding what the path of receipts would have been in their absence.[136]

New tax avoidance and evasion measures

72. In Autumn Statement 2013, the Government announced it would continue to "take further steps to close down avenues for both tax avoidance and evasion, bringing in more than £6.8 billion of new revenue over the forecast period—more than any other fiscal event this Parliament".[137]

73. The Government's 'Autumn Statement 2013: policy costings' document sets out the key areas of uncertainty surrounding each of these policies. In virtually all cases, these areas of uncertainty are those that led to the overestimated yield of the UK-Swiss tax agreement: the size of the tax base, and the behavioural response.[138] Attention was given by the OBR to two of the policies in Table 7 owing to their heightened uncertainty:

> In respect of the specific policy costings at this Autumn Statement, the OBR identified the following areas of particular uncertainty:
>
> [...]
>
> - CGT – amending final exemption period for private residences: The aim of this measure is to reduce abuse of the final period exemption by reducing the time period from 3 years to 18 months. The extra uncertainty arises from HMRC not having a centralised record of the amount this relief currently costs the Exchequer, nor the number of transactions that use it. As with anti-avoidance costings, it is difficult to estimate individual behaviour in response to policy changes.
>
> [...]

135 Treasury Committee, Second Special Report of Session 2013-14, *Budget 2013: Government and Office for Budget Responsibility Responses to the Committee's Ninth Report of Session 2012-13*, HC 370,, p21

136 Treasury Committee, Second Special Report of Session 2013-14, *Budget 2013: Government and Office for Budget Responsibility Responses to the Committee's Ninth Report of Session 2012-13*, HC 370,, p21

137 HM Treasury, Autumn Statement 2013, Cm 8747, 5 December 2013, p9

138 HM Government, *Autumn Statement 2013: policy costings*,, December 2013, pp22-33

- Information Sharing Agreements with Overseas Territories: The estimated revenue raised by these measures is uncertain as there is little hard information about the value and nature of UK individuals' financial assets in these Overseas Territories. There is further uncertainty in the costing around how individuals affected will respond to the policy. Experience with the UK-Swiss tax agreement has illustrated the uncertainties involved in such costings.

Table 7: Costing of 'avoidance, tax planning and fairness' policies

£m	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	TOTAL
Accelerated payments in follower cases	0	+135	+660	-35	-40	-45	**+675**
Onshore employment intermediaries	0	+520	+425	+380	+415	+445	**+2,185**
Dual Contracts	0	0	+85	+60	+60	+65	**+270**
Compensating Adjustments	0	+60	+125	+120	+115	+110	**+530**
Venture Capital Trusts: share buy-backs	0	+50	+35	+10	+20	+25	**+140**
Avoidance schemes using derivatives	+40	+40	+20	+10	0	0	**+110**
Oil and gas: offshore chartering	0	+140	+115	+100	+90	+80	**+525**
Partnerships: confirming extension to Alternative Investment Funds	0	0	+680	+430	+410	+400	**+1,920**
Automatic Exchange of Information agreements with Overseas Territories	0	0	0	+25	+10	+5	**+40**
Double taxation relief: closing loopholes	+10	+20	+5	0	0	0	**+35**
Capital gains tax: amending final exemption period for private residences	0	0	+65	+90	+100	+105	**+360**
Capital gains tax: application to non-residents	0	0	0	+15	+40	+70	**+125**
Corporation tax: change of ownership rules	-30	-10	0	0	0	0	**-40**
TOTAL	**+20**	**+955**	**+2,215**	**+1,205**	**+1,220**	**+1,260**	**+6,875**

Source: HM Treasury, Autumn Statement 2013, December 2013

74. **Every year estimates have to be made of the yield of anti-avoidance measures, in the face of great uncertainty about the outcomes. The OBR itself points out that there is a limit to what can be learned from previous policies in determining whether such costings are suitable. The Treasury Committee warned in 2012 that the proceeds of the UK-Swiss tax agreement might not meet expectations. The Government has reduced its estimate of the expected yield of the UK-Swiss tax agreement by almost two thirds over the course of a year. Given the great uncertainty that surrounds the fiscal effects of tax avoidance measures, the reduction in the estimated yield of the UK-Swiss tax agreement should not be a great surprise.**

75. **The Government has now announced a series of further measures designed to close down avenues of avoidance, each vulnerable to similar uncertainties of their own. In the Government's own words, though, these further measures "will bring in more than £6.8 billion of new revenue over the forecast period—more than any other fiscal event this Parliament". Therefore this perennial problem has now assumed particular fiscal importance given the size of the revenue being forecast. The OBR should do all it can to report on whether yields were attained as originally costed. Where that is not possible, it should limit the extent to which the Government may account for such projected gains.**

6 Transport and energy infrastructure

76. At the time of the Autumn Statement 2013, the Treasury announced an update to its long term infrastructure plan for the UK. The National Infrastructure Plan, first published in 2010 and updated annually, outlines detailed spending plans in a number of areas including roads, railways, telecommunications and energy. It provides a list of priority investments as well as setting out a series of planned public and private infrastructure projects. The National Infrastructure Plan 2013 (NIP) has updated the total value of such investments from £309 billion in 2012 to over £375 billion, [139] of which over £340 billion will be directed to the energy and transport sectors.[140]

Transport spending plans

77. When we last reviewed the Government's infrastructure plans in our Spending Round 2013 Report, we concluded that:

> The Committee welcomes the creation of long term plans for infrastructure investment. It is now crucial that the projects are delivered in a timely and effective manner.[141]

Commenting on the National Infrastructure Plan 2013, Nick Prior, head of infrastructure at Deloitte, said:

> The additional infrastructure funding announced by the Chief Secretary today is welcome but we need much clearer sight of where this money will actually be spent.
>
> The government guarantees scheme is making a difference. This has been the most impactful announcement on infrastructure to date. But, the reality is, little of this money will be spent this side of 2015, so we won't see shovels in the ground on new projects for some time.
>
> The £25bn commitment from insurers is good news in demonstrating the attractiveness of UK infrastructure to investors. But they still need to see a clear pipeline of opportunities to put their money into and this will require some upfront commitment and ongoing funding from government. The intention is there but the funding is still aspirational.[142]

And Jeremy Blackburn, head of UK policy at RICS, said that:

139 HM Treasury, *National Infrastructure Plan 2013*, December 2013, p8

140 HM Treasury, *National Infrastructure Plan 2013*, December 2013, p8

141 Treasury Committee, Third Report of Session 2013-14, *Spending Round 2013*, HC575, para 70, p37

142 www.deloitte.com, Deloitte comments on National Infrastructure Plan update, December 2013

> What is still lacking is real momentum to get these projects moving, even with the £25bn included. It has taken three years of plans to reach a programme. Let's now get on with this – and secure a balanced recovery across all the regions, not just some.[143]

78. We questioned Stephen Glaister, Director of the RAC Foundation and specialist adviser to this Committee, on the delivery of the projects outlined in the 2013 National Infrastructure Plan. He was concerned about the realism of the Government's plan to invest £120 billion in transport projects over the next decade:

> The realism of the Government's plans on their transport budgets generally is a worry over the long term [...] If I look at the announcements that were made in the summer for the three heads of expenditure in the spending review, for the six years starting 2015, the Government committed to spend £22.5 billion on Network Rail, £16 billion HS2 and £15 billion on the strategic road network. I think it is going to be very difficult to find all that money over the years to deliver that, especially since, on the road side, there is no charging mechanism.[144]

Mr Glaister explained that there was a history of road projects not being delivered by government:

> [...] on the road side, we have been here at least twice before. There was the Roads for Prosperity in 1989, which was a big roads investment programme that essentially was not delivered because the Conservative Government of the day could not find the money as they came to the end of their term. There was quite a lot of roads money put into the Labour Government's plans towards the end of their term of office, which was pulled out in the spending review of 2010; including the cancellation of A14 famously, but a lot of roads were pulled out at that time.[145]

Other concerns about highways spending have been noted by Paul Fleetham, managing director of Lafarge Tarmac Contracting:

> Against a backdrop of protracted delays for many large projects, it is disappointing that the updated National Infrastructure Plan fails to provide support for smaller schemes such as essential highways upgrades.[146]

79. We questioned Mr Glaister on the economic merits of High Speed 2 (HS2) and the extent to which the attention given to this project might be resulting in other transport projects being over looked. Mr Glaister said that HS2 "might be taking more attention than perhaps the economic evaluations would suggest is justified."[147] He was particularly concerned about that lack of work assessing the value for money of alternative transport projects:

143 Construction News, *Reaction: National Infrastructure Plan 2013*,4 December 2013

144 Q343

145 Q343

146 Construction News, *Reaction: National Infrastructure Plan 2013*,4 December 2013

147 Q327

> [...] we have not had a decent discussion either inside the Department or more generally about the relative merits using the established scientific methods of appraisal of putting a very large amount of capital into HS2 as against conventional rail or national and local roads. It is HS2 being put on one side, assumed to be there and spoken for, and it has not entered the debate about whether you could spend that money more effectively and indeed spend it more effectively in some other area of public policy.[148]

Mr Glaister explained that the Treasury have "very well-established ways of calculating value for money for different transport investments."[149] Mr Glaister argued that road projects with very high rates of return were not being funded while rail projects which much lower rates of return were. He said:

> [...] there are a number of road schemes, some of which have been funded and I think some of which have not, with benefit cost ratios of seven, eight, nine, 10 and 11; very much higher. On the rail side, I am not aware that the Government publishes cost benefit ratios for rail schemes apart from HS2.[150]

80. **In the interests of transparency of decision-making, the Treasury should set out the absolute benefits and absolute costs, and the benefit:cost ratios, for each road and rail scheme considered by Government, whether approved or not. The calculations should be consistent with well established Department for Transport best practice. This practice is based on Treasury Green Book principles.**

HS2 and contingency costs

81. According to the Department for Transport's report *The Strategic Case for HS2*, the total funding envelope for the HS2 project is £50 billion. This consists of £15.6 billion for Phase One, £12.5 billion for Phase Two, £7.5bn for rolling stock and a £14.4 billion contingency fund (all in 2011 prices, excluding VAT).[151]

82. We questioned Mr Glaister on the rationale of the £14 billion contingency fund for HS2. Mr Glaister wouldn't be drawn on whether the exact figure was correct but stressed the importance of taking a consistent approach for all infrastructure projects:

> The Treasury insists on putting them in because it feels it has had its fingers burnt in the past where an inadequate contingency has been included. Whether it is an appropriate amount or not is hard for me to say. What I would say is it is important that, if the Treasury is going to insist on there being a contingency and there is a case for a certain amount, it is done consistently across the piece because if you are going

148 Q327

149 Q344

150 Q345

151 Department for Transport, The Strategic Case for HS2, October 2013, p 36 &139

> to put in £14 billion for HS2, you need to make sure you put in a proportionate amount in other schemes so they can compare across the piece.[152]

Mr Glaister was concerned about the way contingency funds were calculated and the risk of creating perverse incentives:

> I think the professionals in this field are uncomfortable with the way the Treasury insists on these rather mechanistic levels of contingency in the schemes because they feel they produce perverse incentives. Obviously there is a tendency to think if you have a budget that includes a contingency then you are going to end up spending it. What you should be doing is good, effective costing and binding yourself to effective costs.[153]

83. **The Treasury should ensure that contingency funds are used only for contingencies, and do not become a safety margin to accommodate poor planning.**

UK energy policy

84. As part of our inquiry on the 2013 Autumn Statement we also examined Government's energy policy, particularly focusing on the strategy for decarbonising the economy and the impact this was having on energy infrastructure investment. We asked Peter Atherton, Equity Research, Liberum Capital, whether he believed that the Government had a coherent energy policy. Mr Atherton told the Committee that the UK's underlying energy policy of decarbonising the economy had been "very consistent,"[154] but that the strategy for delivering this policy had vacillated over time:

> We agreed in 2003, as the EU, to go down the path of decarbonising our economies [...] Originally we had some market interventions like the European carbon trading scheme. When the Coalition came in they decided that those interventions that Labour had put into place were not sufficient to deliver the targets. They had a review and out of that has followed electricity market reform and now the current Energy Bill. What you have seen is the number of interventions and the scale of those interventions have increased over time, but the policy goal that was agreed in 2003 at the European level and put into UK law in 2008 in the Climate Change Act has not changed at all.[155]

85. When questioned on whether the Government had an implementation strategy which was both plausible and deliverable Mr Atherton said that the strategy is "extremely unlikely to be delivered."[156] This was because the Government "grossly underestimated the

152 Q349

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economic, financial and engineering challenges of decarbonising a sector like power as quickly as [the Government] are proposing to decarbonise it."[157]

86. Mr Atherton said that by trying to reach the carbon reduction targets the Government signed up to in 2003, energy investment deals were being distorted. He was very critical about the commercial contract agreed in October 2013 between the Government and EDF Energy for the development of the Hinkley Point C nuclear power station:

> Nobody in their right mind would sign an agreement with EDF to fund the economics of an £8 billion reactor that it is going to take them nine years to build [...] and the only reason you are doing it is to deliver the 2030 target. Without the 2030 target you wouldn't do that in any universe I can think of.[158]

He went on to say:

> The inherent complexity and contradictions within the strategy to deliver the goal are coming out, I am afraid. We are seeing that now in the public debate around affordability. I am afraid the affordability crisis that we are seeing in energy policy at the moment in the UK was entirely predictable [...][159]

When asked what the economic cost of the Government's energy policy was likely to be, Mr Atherton estimated that that the net cost of decarbonisation, excluding the investment that would have to occur regardless such as replacing existing infrastructure, would be "in the region of £200 billion–£230 billion."[160] Mr Atherton argued that the Government could either "deal with the issues and the reasons why costs are rising", or it would "have to convince the British public that this is the price worth paying."[161]

157 Q331

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Conclusions and recommendations

The macroeconomy

1. Recent data revisions suggest that GDP has been growing by more than previously thought, and business surveys also suggest that the recovery is taking root. That the recovery is, at the moment, consumer-led, is not surprising. As the Governor of the Bank of England has noted, "recoveries are very seldom, in this country or other countries, led by business investment". However, a broad based improvement in the long run performance of the economy will be required if the recovery is to lead to a long period of trend growth. As we have previously recommended, a greater focus on supply side reform will be required. (Paragraph 18)

The public finances

2. The Committee has previously emphasised the considerable uncertainty in the measurement of the output gap and therefore the limit to its usefulness. The OBR's projection of the cyclically-adjusted current budget, which relies upon a forecast of the output gap, is therefore also highly uncertain. Despite these uncertainties, it nevertheless appears that a significant structural deficit has been the inheritance of the last decade, emphasising the need for further fiscal adjustment. Closing the structural deficit will require an improvement in economic performance. (Paragraph 25)

3. It is not yet clear what the outcome of the Government's review of the Charter for Budget Responsibility will be. It is reasonable to suppose that it may contain amendments to the fiscal mandate. This Committee has previously recommended that any new fiscal framework should be subject to full public consultation. The requirement for the updated Charter for Budget Responsibility, including any amended fiscal framework, to be approved by the House of Commons, falls some way short of this proposal. The Government should consult on any proposed changes to the fiscal framework as part of its review of the Charter for Budget Responsibility. Effective public consultation will improve the prospects of creating a framework for fiscal policy that will be more stable and resilient than those used in the past. (Paragraph 33)

4. Ring-fencing, by definition, requires that the balance of public expenditure restraint and cuts be borne in the rest of public expenditure. Each successive year of public expenditure restraint results in an increase in ring-fenced spending as a proportion of the total. The smaller non-ring-fenced areas in turn have to bear a higher proportion of any savings in subsequent years. The IFS has shown that non-ring-fenced expenditure may fall from 61.6 per cent in 2010–11 to around 50 per cent in 2018–19 of total Departmental Expenditure Limits. Ring fencing also reduces the discipline on spending in these areas: the rigour of negotiations between the department and the Treasury on allocations will be weakened, since it is known in advance by both sides that this spending is protected. (Paragraph 45)

5. The Chancellor says that the ring-fencing of health, schools and overseas aid budgets reflects public preferences. Protection of health and education spending, but not overseas aid, appears to reflect public preferences. (Paragraph 46)

6. The Government should do what it can to ensure sufficiently informed public debate on the trade-offs inherent in ring-fencing and the allocation of spending cuts. Such a debate is especially important in a period of transformative spending reductions. (Paragraph 47)

Housing

7. Data from the end of 2013 indicate that national aggregate house prices have recently been growing at a rapid rate. Mortgage availability, and the demand for mortgages, have both increased. The growth in house prices has drawn considerable public attention, particularly regarding whether the activity yet represents a speculative housing bubble. Witnesses explained rising prices by drawing attention to pent-up demand and the limited supply of housing within the UK, and to the likelihood of a limited short-term supply response to rising house prices. (Paragraph 54)

8. The danger is that it will be difficult for the Financial Policy Committee to identify when a speculative housing bubble may have begun. Such a bubble, driven by increasing lending to households, would be a risk to the UK economy. As the Governor has told us, "experience has shown that imbalances fuelled by a credit boom, which may manifest themselves in asset-price movements, pose the greatest medium-term risk to the economy, because of the powerful deleveraging process they induce when they unwind." House prices are therefore a class of asset price which requires careful attention by policymakers, given their historic and continuing influence on the UK economy. (Paragraph 55)

9. The Committee has previously concluded that the Help to Buy: Mortgage Guarantee scheme could produce negative distorting effects on the housing market. Our judgement has not changed. (Paragraph 60)

10. In addition to this, the Government's Help to Buy: Mortgage Guarantee scheme may have further distorting effects on the UK housing market when withdrawn. The Treasury should examine the impact of an abrupt end to this scheme, and act in advance to mitigate market distortions before they arise. The Government should explain now what the exit strategy from Help to Buy: Mortgage Guarantee will be in order better to influence expectations. The Bank of England may need to adjust the timing of its regular annual review of the Help to Buy: Mortgage Guarantee scheme accordingly. (Paragraph 61)

Individual measures

11. The Treasury's analysis of the dynamic effects of the Government's corporation tax cut is subject to great uncertainty. Nonetheless, there is some merit in continuing to study the dynamic effects of policy decisions. It is important to emphasise, however, that the OBR took account of some of the effects of the Government's corporation tax cut discussed in the Treasury's paper in its own forecasts, including the effects on business investment and profit shifting. The OBR has stated that the Treasury's

analysis has not affected its official economic forecasts. We will expect the OBR to continue to reach its own independent judgement on the effects of tax changes on the yield. (Paragraph 66)

12. Every year estimates have to be made of the yield of anti-avoidance measures, in the face of great uncertainty about the outcomes. The OBR itself points out that there is a limit to what can be learned from previous policies in determining whether such costings are suitable. The Treasury Committee warned in 2012 that the proceeds of the UK-Swiss tax agreement might not meet expectations. The Government has reduced its estimate of the expected yield of the UK-Swiss tax agreement by almost two thirds over the course of a year. Given the great uncertainty that surrounds the fiscal effects of tax avoidance measures, the reduction in the estimated yield of the UK-Swiss tax agreement should not be a great surprise. (Paragraph 74)

13. The Government has now announced a series of further measures designed to close down avenues of avoidance, each vulnerable to similar uncertainties of their own. In the Government's own words, though, these further measures "will bring in more than £6.8 billion of new revenue over the forecast period—more than any other fiscal event this Parliament". Therefore this perennial problem has now assumed particular fiscal importance given the size of the revenue being forecast. The OBR should do all it can to report on whether yields were attained as originally costed. Where that is not possible, it should limit the extent to which the Government may account for such projected gains. (Paragraph 75)

Transport and energy infrastructure

14. In the interests of transparency of decision-making, the Treasury should set out the absolute benefits and absolute costs, and the benefit:cost ratios, for each road and rail scheme considered by Government, whether approved or not. The calculations should be consistent with well established Department for Transport best practice. This practice is based on Treasury Green Book principles. (Paragraph 80)

15. The Treasury should ensure that contingency funds are used only for contingencies, and do not become a safety margin to accommodate poor planning. (Paragraph 83)

Formal Minutes

Wednesday 5 March 2014

Members present:

Mr Andrew Tyrie, in the Chair

Mark Garnier
Andrea Leadsom
Mr Andrew Love
John Mann
Mr Pat McFadden
Mr George Mudie
Teresa Pearce
David Ruffley

Draft Report (*Autumn Statement 2013*), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 86 read and agreed to.

Resolved, That the Report be the Ninth Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Tuesday 11 March at 9.15am

Witnesses

The following witnesses gave evidence. Transcripts can be viewed on the Committee's inquiry page at www.parliament.uk/treascom.

List of written evidence

Written evidence can be viewed on the Committee's inquiry page at www.parliament.uk/treascom.

1 Institute for Fiscal Studies

2 Institute of Chartered Accountants in England and Wales

List of Reports from the Committee during the current Parliament

Session 2010–12

First Report	June 2010 Budget	HC 350
Second Report	Appointment of Dr Martin Weale to the Monetary Policy Committee of the Bank of England	HC 475
Third Report	Appointment of Robert Chote as Chair of the Office for Budget Responsibility	HC 476
Fourth Report	Office for Budget Responsibility	HC 385
Fifth Report	Appointments to the Budget Responsibility Committee	HC 545
Sixth Report	Spending Review 2010	HC 544
Seventh Report	Financial Regulation: a preliminary consideration of the Government's proposals	HC 430
Eighth Report	Principles of tax policy	HC 753
Ninth Report	Competition and Choice in Retail Banking	HC 612
Tenth Report	Budget 2011	HC 897
Eleventh Report	Finance (No.3) Bill	HC 497
Twelfth Report	Appointment of Dr Ben Broadbent to the Monetary Policy Committee of the Bank of England	HC 1051
Thirteenth Report	Appointment of Dr Donald Kohn to the interim Financial Policy Committee	HC 1052
Fourteenth Report	Appointments of Michael Cohrs and Alastair Clark to the interim Financial Policy Committee	HC 1125
Fifteenth Report	Retail Distribution Review	HC 857
Sixteenth Report	Administration and effectiveness of HM Revenue and Customs	HC 731
Seventeenth Report	Private Finance Initiative	HC 1146
Eighteenth Report	The future of cheques	HC 1147
Nineteenth Report	Independent Commission on Banking	HC 1069
Twentieth Report	Retail Distribution Review: Government and FSA Responses	HC 1533
Twenty-first Report	Accountability of the Bank of England	HC 874
Twenty-second Report	Appointment of Robert Jenkins to the interim Financial Policy Committee	HC 1575
Twenty-third Report	The future of cheques: Government and Payments Council Responses	HC 1645
Twenty-fourth Report	Appointments to the Office of Tax Simplification	HC 1637
Twenty-fifth Report	Private Finance Initiative: Government, OBR and NAO Responses	HC 1725
Twenty-sixth Report	Financial Conduct Authority	HC 1574
Twenty-seventh Report	Accountability of the Bank of England: Response from the Court of the Bank	HC 1769
Twenty-eighth Report	Financial Conduct Authority: Report on the Governments Response	HC 1857
Twenty-ninth Report	Closing the tax gap: HMRC's record at ensuring tax compliance	HC 1371
Thirtieth Report	Budget 2012	HC 1910

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First Report	Financial Services Bill	HC 161
Second Report	Fixing LIBOR: some preliminary findings	HC 481
Third Report	Access to cash machines for basic bank account holders	HC 544
Fourth Report	Appointment of Mr Ian McCafferty to the Monetary Policy Committee	HC 590
Fifth Report	The FSA's report into the failure of RBS	HC 640
Sixth Report	Appointment of John Griffith-Jones as Chair-designate of the Financial Conduct Authority	HC 721
Seventh Report	Autumn Statement 2012	HC 818
Eighth Report	Appointment of Dr Mark Carney as Governor of the Bank of England	HC 944
Ninth Report	Budget 2013	HC 1063

Session 2013–14

First Report	Appointments of Dame Clara Furse, Richard Sharp, and Martin Taylor to the Financial Policy Committee	HC 224
Second Report	Appointments of Dr Donald Kohn and Andrew Haldane to the Financial Policy Committee	HC 259
Third Report	Spending Round 2013	HC 575
Fourth Report	Re-appointment of Professor Stephen Nickell to the Budget Responsibility Committee	HC 688
Fifth Report	Appointment of Sir Jon Cunliffe as Deputy Governor of the Bank of England	HC 689
Sixth Report	Re-appointment of Dr Martin Weale to the Monetary Policy Committee	HC 313
Seventh Report	Money Advice Service	HC 457
Eighth Report	OBR Fiscal Sustainability Report 2013	HC 958
Ninth Report	Autumn Statement 2013	HC 826