



HOUSE OF LORDS

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Inquiry on

THE ECONOMIC CASE FOR HS2

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Questions 256 - 262

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5.10 pm

Witness: Jim O'Neill

Members present

Lord Hollick (Chairman)
 Baroness Blackstone
 Lord Carrington of Fulham
 Lord Griffiths of Fforestfach
 Lord Lawson of Blaby
 Lord May of Oxford
 Lord McFall of Alcluith
 Lord Monks
 Lord Rowe-Beddoe
 Lord Shipley
 Baroness Wheatcroft

Examination of Witness

Jim O'Neill, Chair, City Growth Commission

Q256 The Chairman: Mr O'Neill, thank you very much for joining us. I am sorry we are starting a few minutes late, but I hope you found the session with Sir David as interesting as we did. Can I just start off by reporting some evidence that we received from Emile Quinet, the French transport economist? He said that if you evaluate the economic benefit of the TGV, it largely accrues to Paris. It is the capital city that wins the day. Would you not have that concern: that it would suck more economic activity down to London? We have heard in the previous session that some have suggested that Birmingham will simply become a commuter city for London. If that is the case, it will be difficult to fulfil the ambition your growth commission has of stimulating growth within the Northern Hub.

Jim O'Neill: Can I just say quickly, before I answer the question specifically, that I am doing this with three things in my mind? First, most of my experience is as a macroeconomist. Secondly, I am also the chair of the City Growth Commission, which, if you are not aware, has now formally finished, but it lives on, given the topicality of many of the issues. Thirdly, in a probably much less relevant way than either of those two, I am somebody from Manchester who has been up and down from Manchester to London for more than 30 years. Yes, I would sympathise with that.

The Chairman: When you had your growth commission, did you consider the relative impact of HS2 on the north and on London?

Jim O'Neill: Before I accepted the role of chairing it, I inquired as to whether those that were proposing the commission had a view as to the importance of HS2 to our commission. The answer was, "Why is that so important?". I said, "Well, I predict it will probably be the first question I get asked when I have a press conference. For that reason, we probably, if possible, should have a stance". Listening to some of what you discussed earlier, knowing that a number of northern cities were in favour, it was not entirely clear to me—and this is why I said the three things earlier—why, especially from a macroeconomic perspective, it was so clearly beneficial.

When we got into the work of the City Growth Commission, it certainly seemed to me that if you are going to spend what is 2.5% of current GDP, it might not be the most efficient thing to do, certainly not in terms of the purpose of the City Growth Commission, which looked and lives on to look at things to try to promote stronger urban growth outside of London—not at London's expense, I quickly add. It did not and it still does not strike me as being clearly that beneficial.

The Chairman: We have had quite widely divergent opinions from economists who have been witnesses, but we have much more of a consensus on local connectivity—the

agglomeration effect, if you like—which London benefits from enormously, appearing to be a very strong driver of economic growth.

Jim O'Neill: Relatively early on in our process, we went around the country having hearings, and at the one we had in Manchester I was shocked—I had and still have a lot of ignorance about many of these issues around the country—to hear how they are still debating electrification of some of the lines between northern cities. That really solidified in my mind that if we were trying to pursue interventions that may have some influence on these hugely powerful trends that have gone on for decades of London strength relative to elsewhere, we had to think about pretty bold things. It seemed obvious to me that, when you have what I have weirdly ended up describing as ManShefLeedsPool and all those urban areas within that area, a population similar to the size of London, an absolute minimum thing is to connect them all in a vastly better way than they are today or in a way that was even being thought about until we suggested it.

Q257 Baroness Blackstone: I just want to ask you a question in relation to your position as a macroeconomist. Given the fiscal constraints at present, do you think, as a macroeconomist, it makes sense to spend £50 billion on this project? If you do not, could you tell us why you think the Treasury has agreed to put this sort of money aside for it?

Jim O'Neill: Oh dear. As I said earlier, 18 months ago, just ahead of the City Growth Commission starting, it did not seem to me from a risk management perspective, at a time of preserving our credit rating and effectively undertaking that sort of fiscal stimulus on the official balance sheet, that it was that wise. In terms of the clear macroeconomic benefits, I thought it was questionable.

Baroness Blackstone: Do you still think that? Do you still question the wisdom of this investment from that point of view?

Jim O'Neill: Now, this links with a question that was asked earlier. With the very enjoyable experience that I had of chairing the City Growth Commission, I think that if one were going to have the luxury—sorry, let me give you two answers. As one of the very experienced local authority experts said in our debate about this when I raised this subsequently, the reality is that once there is some vague coalition of national leadership about some big project, why waste time trying to pull it apart, because it is not obvious that you would get something else as an alternative. That sounded like quite an interesting view from somebody who has probably spent a lot of time on some of these kinds of issues, and I emphasise that I have not. It still seems to me to be a large amount of money, and certainly with my cities growth hat on—I was always working on £42 billion, but I have heard you all say £50 billion now—

The Chairman: That was in 2010 prices.

Jim O'Neill: I said to the Core Cities Group that if you divvied up £42 billion between what was seven at the time—that has now expanded as a group, of course—you could probably find greater mutual economic benefit from that. Of course, from a macroeconomic perspective, since then one of the most intriguing things, despite the economy cyclically recovering so well, is that the fiscal position has not because of the uncertainties about an apparent decline of the tax base, so the issues would be even stronger.

Baroness Blackstone: Is it not a bit of a cop-out to say that there are no other alternatives that might be better projects to spend this money on, as you were implying just now?

Jim O'Neill: Why is it a cop-out?

Baroness Blackstone: Because clearly if you give enough consideration to it, there are alternative infrastructure projects to HS2.

Jim O'Neill: Take the Northern Hub. I do not know the latest estimates, but from the numbers that I have seen coming from the group that has put that together, it is much less. In terms of influencing the growth trend of the UK, if you had to choose between the two, it would be better.

Q258 Baroness Wheatcroft: Were you intrigued, as I was, to hear Sir David talk about the fact that London was very good at lobbying, and maybe the north should make its voice better heard? I thought it was a strange thing to say, particularly as he then referred to national infrastructure and to east-west as some sort of add-on that was not part of national infrastructure. Do you think that what he was implying, really—that everything that goes on in this country is London-centric, including the thinking—is at fault, and conjures the view that national infrastructure has to be about London?

Jim O'Neill: I chuckled quite a bit when I heard that question and some of the answers. I will say a perhaps slightly odd-sounding thing to start with. One of the interesting things that we found, going through the commission, is that trying to encourage many local authorities to be more ambitious and to think outside of their comfort zone was one of the really enjoyable aspects of it. For other reasons or things that we have been involved in, I think we are actually going through that process. It has become so popular to say that I think it is justifiable. The Greater Manchester thinkers about these things are quite bold. I would imagine that some people involved in London councils would question whether, while decisions might be being made in London, they are necessarily benefiting London more than the regions. I do not know.

From my experience, it may reflect my home bias, but I think that the local authorities that are the most bold and that articulate the case the strongest, as we have seen in the past six to nine months with the Chancellor's response, get an ear.

Baroness Wheatcroft: You very much made the case for the Northern Hub and connecting those cities. Do you think that as part of the localism agenda and maybe delivering that that municipal bonds might be something we should be looking at?

Jim O'Neill: Definitely. It did not get as much attention from our proposals as I thought it might, and it was in my mind straight from the start that that would appear to be a logical idea to pursue.

Baroness Blackstone: Have you had any response from Government about that?

Jim O'Neill: Less interest in that than some of our other ones. When there has been discussion, it has been due to concerns about the credit rating, which is intriguing, given the earlier question.

Q259 Lord May of Oxford: I have an implausibly extreme suggestion to put to you, which will probably amuse you, I do not know.

Jim O'Neill: That sounds exciting.

Lord May of Oxford: We have just had, as you know, I think quite a good session. Nonetheless, the more I have learnt about HS2, the more I feel that—this bloke we just had was not an example—many of the people involved in it I would not trust to mow my lawn, much less build a big thing like HS2. I am rather taken with your report, where you say you first worried about the thing being all concentrated on this and that your focus was really more on the second phase and thinking broadly about connectivity between the major northern cities, via faster train things, as being a much more useful thing to do. I find that a very persuasive argument.

If I were the supreme dictator and in charge of all this, I would be connecting up all the cities there first and letting them get down to London however they wished to. I would have turned the whole thing upside down. I wondered what you thought of the probability of that happening, because unfortunately I am not. I would be a much better supreme dictator than the current Government.

Jim O'Neill: I have two comments. I think I heard David Higgins say that his guess is that you could not get legislation through until 2021. I have no knowledge of the British legislative process, but that was extremely worrying and disturbing to hear, in my opinion.

I should add, as an important thing, that a number of northern cities get quite irritated with me when I say, with the clarity that I hope I just had a minute ago, that doing things, connecting

all these places together, is in my judgment way more important than them to London faster than it is today. They get quite annoyed with me, because they want both. Maybe they think they are not going to pay for it either. In my judgment, if the purpose is to think about helping those urban areas to grow more, and if it is done just in its own right or to balance the contribution to national GDP, it would be great if it was done the other way round, in my view. A lot of people get very annoyed with me saying that.

Lord Monks: On the point that was raised by Baroness Wheatcroft about bonds, which was in your report, you mentioned that the Government have not nibbled a little bit at that idea. What about the northern cities themselves? Is that something that they are pressing hard for? Are they looking to re-establish the old days of municipal bonds, which my mother and father and others used to invest in, and so on?

Jim O'Neill: I would say that it is something they are supportive of and in favour of—not banging the table about, for reasons I am not entirely sure about, but certainly in support of and would welcome.

Lord Monks: But not banging the table, not putting it up as their priority.

Jim O'Neill: What has, of course, become the thematic concept of our time is this so-called earn-back model, which is quite complex in some parts, so much so that I am still not entirely sure I fully understand that much of it, but it is where they get some grant or relief now for more autonomy over expenditure that they pay back later. There are two things. With that, the whole notion of a combined authority has become so popular that many local areas are wanting to become combined authorities, because they know that is the only way of getting an ear.

It might well be that the focus on municipal bonds as a realistic thing to do has been lost in the practical reality that this is the theme of the moment. It is a little surprising to me that there was not more banging of the table about that.

Q260 Lord Monks: My other question is about this north-south versus east-west debate that we have been having. How would you react to this question? The overwhelming economic logic is that London and the south-east of England are the growth part of the country, which, with sinews, can spread out and spread its influence, particularly, perhaps, as far as Birmingham, and that the northern connections are between places that, frankly, are not very successful. They have limited ambitions, which I think I heard you say at some stage in the past was the case; I do not think it is the case so much now. They had a lousy 20th century, with the collapse of their staple industries, and only got going in the 1990s, I would say.

What are the economics of spending a lot of money connecting cities that, on their own, need a big subsidy from the south-east of England? As you see in existing stations, the smart train is the one going to London. That is the long one, the one with 12 carriages, is it not? The others—

Jim O'Neill: They probably have two on.

Lord Monks: They have two on, going to Leeds, and are not always full. It would be very nice to see what Lord Lawson calls a northern Crossrail, but the economics of it are perhaps even shakier than they are of HS2.

Jim O'Neill: Let me say three things in response to that, perhaps sounding initially not necessarily connected. The first and most important thing, going back to the mindset of myself as the chair of the City Growth Commission, is that I acknowledged at the outset that there are very powerful forces, which have been going on for a long time, that are very beneficial to London, and in some cases at the expense of other urban centres. I often describe London, as some of you are aware, as being the BRIC capital of the world. I think this is a remarkably fantastic time for London's role in the world, as the world's best located major city, and it is very difficult and it may not be very wise to try to stop those things, because it is great for London and it probably spreads out help for the nation.

The second thing is that, with that in mind therefore, if you are tasked with looking at things to help other urban areas, you have to think a bit if not necessarily unconventionally then certainly boldly and a bit out of the box. Connecting the two together, among the many reasons why London is doing so well is, of course, the sheer agglomeration benefits that come from virtuous circles of transport, young people, ideas. The thing that slightly started me on this path, reflecting my background, is that on occasional visits to Manchester to give talks about various matters over the years I have noticed that there were more people from Liverpool in the audience, where in the early days there would not, so there is some sort of thing developing between these places in a way that 20 years ago would not.

I might be incorrect, so apologies if this is the case, but I am conscious of something that I think I heard Mr Higgins say. Unfortunately, we got this data after we had finished our final report. There is quite a rise in commuting going on between Manchester, Leeds, Sheffield and Liverpool, in particular going into Manchester and Leeds from both those cities, but especially from Leeds and Sheffield. Those things are going on already. In my judgment, influenced by my history in markets and finance, the best interventions are when the trend has turned or is turning, so you have some things going on there that in the past, with the challenges you describe, were not. If it were not for feeling things like that, I would have

been more reluctant to support such ideas, for the reasons your question said, but it seems to me, if you can explore non-too-expensive ways of trying to boost connectivity between those very closely geographic urban centres, you can probably get some agglomeration benefits that otherwise you cannot.

Lord May of Oxford: It is worth remarking that there are some excellent universities there—

Jim O'Neill: A just as important part of our recommendations as the transport thing was this—

Q261 Lord Griffiths of Fforestfach: I wonder if you can comment on something that has come up in the evidence we received. On the one hand, people have come and said, especially from Government so on, “We have done cost-benefit analysis. Cost-benefit analysis says that this is a positive return”. When you go back to exactly what the cost-benefit was, a lot of it was about how much travel time was saved and so on, and you begin to feel that if we are really talking about the growth of the north and so on it gets a little flimsy. However, they are saying, “We follow the best methodology we can”. Then there are other people who, when questioned, although they would not start saying this, in the end you have to conclude are really saying that it is a punt—that frankly cost-benefit can take you so far. Cost-benefit is great when you have a discrete project over a short period of time, like any private investment proposal, but when you are talking about 60 years and, as we heard earlier today, a national transport strategy within which you should be fitting anything, this is not something, in my judgment, that cost-benefit analysis was ever really intended to solve. Let me just say there is a strain of thought that says, “Frankly, this is really a punt”, and if you are relying on the economic case to do it, it is quite hard to really say this is a cast iron economic case. What is your response to that?

Jim O'Neill: I am going to do the dreadful economist thing and answer you in a different way. When we looked at ideas for the City Growth Commission that we would end up formally recommending in our final report, our premise was: could it improve the long-term growth potential of the UK economy? We were not looking at any of the individual cities. We defined 15 metro areas outside of London, but we wanted to do it in the context of: whatever cost or money might be spent, would it boost the long-term growth rate? In fact, we ended up suggesting that if things could be done to have all these 15 areas growing at the rate that London had grown, the UK’s national growth trend could be increased by 0.2%, up to 2030. That still seems to be the right framework. That would be the way that I would look at something like that. You would want to look at the whole rationale behind HS2, if I had been involved in it—and let me reiterate that I have never really looked at HS2 itself at all, other

than in the context of the reasons I gave—in that context. I would say in that regard that we spent some time on this, as we did in our discussions with policymakers, including the Treasury, and luckily there are now some signs of flexibility or shift on that, because of the very powerful focus on it from the Chancellor, in my view. So much analysis is done on: “It is going to cost X. That means that is going to come from somewhere else”, and there is not really any focus on any supply-side benefits that might come, which is why we were deliberately eager to pursue it that way. But I would not have approached HS2 with a standard cost-benefit analysis, full stop.

Lord Lawson of Blaby: I think the way you have just spoken about it really is totally fanciful.

Jim O'Neill: Some might say economics is totally fanciful.

Lord Lawson of Blaby: Well, economics is dodgy, but we do not have time to go into a critique of macroeconomics. We can do that some other time maybe, in some other forum. But regarding the idea of thinking the cities of the north grow at the same rate as London, it is fine to say the cities of the north have not fulfilled their potential. Maybe there are ways in which transport can help there. In particular, I would have thought—incidentally, you have not mentioned these—there are the freight links along the north, with the importance of the ports, of Liverpool in the west and Hull in the east, and getting goods to the ports. But the fact is that this is chalk and cheese. The cities of the north are British cities. London is not a British city. London is a global city located in Britain. If global growth is likely to be greater than UK growth, it stands to reason that it is more likely than not that London will grow faster than the north. Whatever you do with railway trains is not going to change that. It is a fundamental factor of the nature of London. As I say, it is not really a British city at all. Is it not really completely fanciful to put it in the terms in which you have put it?

Jim O'Neill: I agree with everything you have said, apart from that last phrase. As I said earlier, I think of London as being the BRIC capital of the world, and it is a fantastic time for London's position in the world. However, does that mean one should not do anything to try to influence the future of non-London urban growth?

Lord Lawson of Blaby: No. I said explicitly that we should think of what can be done to improve the efficiency and effectiveness of the great northern urban centres, but you said that if the north could grow as fast as London, why should it not, and somehow what you were about was designed to achieve that. What I am saying is there is a fundamental reason why that comparison is false.

Jim O'Neill: I am conscious of you guys having homes to go to and things to do, but I am happy to pursue anything you want to in this regard. Let me say three things about that. First of all, there is a difference between size and rates of growth. We did not just look at the north. People often think that we looked at the north, because the Chancellor took up a lot of our ideas and is running with them for the north, and it has obviously become a focal point. But we identified the 15 largest populated metro areas outside of London, which included Glasgow, Edinburgh, Belfast and the other 12. Bristol is a very interesting place, where we had one of our hearings. Bristol has a higher GDP per capita and gross value added, as it is described, than the average of the UK. It is a very successful city. In the past couple of years, some of these places have grown by more than London. It does not necessarily follow, just because London is in this great position of benefiting from the world, which I agree with, that it is necessarily always going to grow by more than all these other places, not least because it does not.

Secondly, very importantly, transport, the east-west and what has now become One North, was one of our important recommended interventions, but it certainly was not the only one. Just as important, in my opinion, is thinking about the knowledge base coming out of the northern universities. The other thing that has followed from the interest in them is what people call the northern answer to the Crick. It is the idea of this collaborative research institute, which is going to be Manchester-based again. That is just as important, in my judgment, as the transport links. Devolving the whole skills responsibility is especially important, and of all the things that people focus on in devolution, that one in our judgment was the most easy to recommend devolving away from Whitehall. There is also a whole host of other things, so it certainly was not just about transport, but transport would be an important part of it.

Q262 Lord Carrington of Fulham: I found Sir David Higgins' evidence very interesting, but one of the things I found most interesting in it was his throwaway line that he was moving HS2 up to Birmingham. There may be other reasons, but the only reason he gave was, of course, that the property prices in Birmingham were half the value that they were in King's Cross, which told me that what he was really doing was not tapping into a skill base in Birmingham that did not exist in London but going for a cheaper cost base in Birmingham—in other words connecting Birmingham into the greater economic area of London. It did seem to me that that rather jibed with what we have been hearing about the potential impact of HS2—that effectively, as some people say, it will bring Birmingham into the commuter belt of London, but it is much bigger than that. It brings it into the economic sphere of London,

and as presumably it comes to Manchester and Leeds, and you get an hour's travel time from Manchester to London, as we were hearing, which I must say is a rather shorter commuter time than I thought it was going to be—

Jim O'Neill: I thought it was one hour and 20 minutes from Manchester.

Lord Carrington of Fulham: I thought it was nearer one and a half. Nevertheless, it makes travelling from Manchester to London commutable, and so it effectively will bring all these cities into the whole nexus of the London economic area, and, as we were hearing, the global area. Is that how you would see it working? It seems to me that we are not then creating two economies in the UK; we are potentially creating one economy but based on the London model covering the whole country.

Jim O'Neill: Again, I may have three possibly unconnected responses. I said at the start that I was answering your questions with three experiences, one of which was as somebody who has travelled from Manchester to London and back for more than 30 years, and today two hours 15 seems like the world's greatest travel compared with what it used to take 30 years ago.

Lord Carrington of Fulham: Absolutely. I remember it well.

Jim O'Neill: It is not entirely obviously to me that reducing that time has done a lot for Manchester. Obviously, it is a lot easier for people to get here than it used to be.

Secondly, and there may be some connection, that is great for those who have education and the capability to participate in that part of life, but one of the reasons why issues like skills are so important, and that part of the City Growth Commission, is what about all those that cannot? Indeed, if you look at some of the things going on in inner Manchester and Leeds right now—I would highlight those two from my limited knowledge as perhaps two of the most successful in the north—there are some positive things going on there that benefit again those who have the right education, the right skill set, but of course there are severely challenged inner urban areas where there is no benefit at all, and they are not going to get any benefit whatsoever from any of these things. It was interesting to hear the unfortunately very brief discussion about the price; one would imagine it is going to be some kind of premium price, and the potential beneficiaries of that would be quite narrow, in terms of the broader macroeconomic benefit.

Thirdly, I am aware of an economist that works in a macro hedge fund who coincidentally, when we launched the commission, had this very interesting report—I am not quite sure why he was writing about cities—arguing that over the long term HS2 would be a key towards

equalising UK house prices. Now, if one could believe that, that would be fantastic; one would think that would be a really powerful consequence.

Lord Carrington of Fulham: What I am getting out of a lot of the evidence we have heard, and I value your view on it, is that this is one of those projects where nobody knows what it would do—that nobody really has any idea what effect putting in this high-speed train will have. It is rather like throwing a stone into the middle of the pond. Nobody knows where the ripples are going to go and what impact it is going to have on the banks or anything. It is just: “Put the money in, put the thing in, because spending that amount of money on something like that has to produce some good, has it not? Keep your fingers crossed, tuck your trotters up, and trust to luck”.

Jim O'Neill: I am not sure how to respond to that. Part of me thinks that maybe we do need a bit more ambition about some of the things we do in this country. Yes, I am very sympathetic to all of that, but to change the supply side of the country, maybe we need bolder things. Whether this one is the right one, as I have made clear, I do not think so.

Lord Shipley: I just wanted to pursue the question of the development impact of private sector investment, which it has been said to us will follow where the new track is. There is another school of thought that says that, actually, to have the rolling stock on existing lines can be significant in encouraging people to invest where there is not a new track. Did you do any work at all on the impact of HS2, with its new track, on places like Teesside, Newcastle and the North East, where I come from, Carlisle, Preston, Liverpool and Hull? Much of the discussion taking place around HS2 is talking about Manchester, Sheffield, Leeds and, to a degree, Liverpool, but there are a lot of people living in those other areas.

Jim O'Neill: No, we did not. As I said, we did not look at HS2 specifically itself, but its proposal and existence contributed to us thinking about other transport improvements. One thing I meant to say, as we heard from a gathering we had at the Conservative Party conference in Birmingham, is something called Midlands Connect would strike me as quite interesting as well, insomuch as there is so much focus on One North. We did not look at that; we did not look at HS2 directly in that sense. There is one quick thing to add: I am more than aware of that from a number of smaller cities, including some that you mentioned, that chased me around the country and berated me for not thinking about them in our selection of the 15 largest metro areas—some of them rather well.

The Chairman: Thank you very much indeed for joining us, and it was a very interesting perspective on the work that your commission has done, which certainly has quite a lot of bearing on some of the issues that we are going to be reporting upon. Thank you very much.

Jim O'Neill: Thank you very much.