HOUSE OF COMMONS

Treasury Committee

Oral evidence: Work of the Treasury, HC 137

Monday 12 December 2022

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Watch the meeting

Members present: Harriett Baldwin (Chair); Rushanara Ali; Mr John Baron; Anthony Browne; Dame Angela Eagle; Danny Kruger; Dame Andrea Leadsom; Anne Marie Morris.

Questions 99-226

Witnesses

I: James Bowler CB, Permanent Secretary, HM Treasury, Anna Caffyn, Finance Director, HM Treasury, Phil Duffy, Director-General, Growth and Productivity, HM Treasury, Cat Little, Second Permanent Secretary, HM Treasury and Beth Russell, Second Permanent Secretary, HM Treasury.

Examination of witnesses

Witnesses: James Bowler, Anna Caffyn, Phil Duffy, Cat Little and Beth Russell.

Q99 **Chair:** Welcome to this session of the Treasury Committee on the work of the Treasury. We are joined by three witnesses in the Committee Room and two remotely, one from the Darlington campus and one due to snow problems, I believe. I will ask our witnesses to introduce themselves, starting with you, James.

James Bowler: I am James Bowler, permanent secretary at the Treasury.

Anna Caffyn: I am Anna Caffyn, finance director at the Treasury.

Phil Duffy: I am Phil Duffy. I am the director-general for growth and productivity at the Treasury.

Beth Russell: Hello. I am Beth Russell. I am second permanent secretary at the Treasury.

Cat Little: Hello. I am Cat Little. I am second permanent secretary at the Treasury.

Q100 **Chair:** It is good to see you all. For the record, DEC stands for Darlington Economic Campus. James, I congratulate you on your appointment as permanent secretary. I believe that it was announced on 10 October that you were starting. Was that the day you got your feet under the desk?

James Bowler: Thank you very much. Yes, 10 October starting. I think I was supposed to start on 17 October, but I did indeed start on 10 October. By 17 October, there had been two reversals in policy on the growth plan, so it was a busy first week.

Chair: You started on 10 October—

James Bowler: I did.

Q101 **Chair:** And you were involved in those reversals, presumably.

James Bowler: Yes.

Q102 **Chair:** To clarify further for the record, I thank Beth and Cat, who were both acting permanent secretaries during the interregnum, because Tom Scholar left on 8 September, I believe. Is that right?

James Bowler: Yes, that is right.

Q103 **Chair:** Is it normal for there not to be a handover like that?

James Bowler: No. Tom's departure was not normal. For the record, what happened was that the then Chancellor of the Exchequer said that he did not want Tom to continue as permanent secretary, so Tom stood aside. The process was undertaken to appoint someone in his stead through the Civil Service Commission, but at relative speed, so Tom left on 8 September and I started on 10 October.

Q104 **Chair:** Perhaps I can ask Beth and Cat about this. When Chancellor Kwarteng started on 5 September, had it become clear to you over the summer that you were going to experience the departure of Sir Tom Scholar, or was it a shock?

Beth Russell: No, we were not aware of that. Both Cat and I found out on the day that Tom left.

Q105 **Chair:** Not till 8 September, then.

Beth Russell: That is correct.

Q106 **Chair:** Had there been a procedure in place whereby you both would step up to be joint permanent secretaries in the event of the permanent secretary not being there?

Beth Russell: No, that was decided on that day, I think in consultation between Tom, before he departed; the Cabinet Secretary, Simon Case; and the Chancellor at the time. Cat and I stepped in together to take over in the temporary period.

Q107 **Chair:** James, you have said it's unusual for a transition to happen in this way. Was there a cost to the taxpayer in terms of a severance package for the previous permanent secretary that was not budgeted for?

James Bowler: Any severance package will be in our annual report and accounts next year. I am not privy to that particular detail in terms of what happened with Tom; that's not my decision.

Q108 **Chair:** Was it you who commissioned the Office for Budget Responsibility to prepare their forecasts, on your first day?

James Bowler: No. At that point, a decision had been taken to split how we were going to do the fiscal events into two different parts, so there was the growth plan, which happened on 23 September, and that was going to be followed by a medium-term fiscal plan on 31 October. I think it was announced at the start that the OBR would have a forecast by the end of the year, and then it was clarified that that would inform that medium-term fiscal plan on 31 October. So the growth plan came first, on 23 September, and the OBR forecast was going to follow. That was the proposal of the then Chancellor.

Q109 **Chair:** Beth, you were informed about Sir Tom Scholar's departure on 8 September and you were told that there was going to be a fiscal event on 23 September, or did you already know that, and that you and Cat were running the ship?

Beth Russell: I believe—Cat can correct me if I'm wrong—that the fiscal event date at that point had already been announced. Cat and I obviously took over running the Department at that point and dividing it up between us.

Q110 **Chair:** How much of what was announced on 23 September were you fully sighted on as acting permanent secretaries?

Beth Russell: We were fully sighted in the normal way, and the advice process took place in the normal way. Obviously, we did not have an OBR forecast for that event, so the process was slightly different as a result of that, but we were fully aware of the measures in the event.

Q111 **Chair:** In giving that advice, did you score it in the normal way, or did you take into account the way in which it might interact with some of the market movements, or did you just score it as if it wouldn't move the market?

Beth Russell: There are a couple of things here. First, in terms of giving advice on the costs of measures, in a normal event, where there is an OBR forecast, the OBR would certify the costings of all measures. That bit did not happen, but we gave advice on the costs of all the measures in the event in the way we would normally do. Cat and I are confident that we gave all the advice that we should have done to Ministers on the economic and fiscal backdrop, on the impacts and the market position, and particularly around the financing requirement, which was a big issue because of the cost of the measures.

Q112 **Chair:** So you did flag that there might be risks around the financing requirement.

Beth Russell: We did, yes.

Q113 **Chair:** Was there anything more that you could have done? I suppose, really, your role stops at just flagging what the potential risks are for the Chancellor in taking the steps that he is planning to take.

Beth Russell: Ultimately, the decisions are for Ministers. It is our job to make sure that we give the best advice possible on the impacts and the consequences, and I think that we both feel that we did that on the situation in the markets, particularly around the differing market expectations of the size of the package at that event relative to what was announced.

Q114 **Chair:** What is your assessment of what the market expectations were on the eve of 23 September?

Beth Russell: From memory, I think it was a loosening of between £25 billion and £30 billion. I think the eventual package was around £45 billion.

Q115 **Chair:** Thank you. James, may I ask you about morale? Obviously this has been, I would imagine, quite traumatic for your team of officials going through these unprecedented changes, in terms of not only personnel but the market reaction and so on. How would you assess morale at this point?

James Bowler: It has been a tough year, I think, for Treasury civil servants. There has been a lot of crisis upon crisis—covid, Ukraine and energy. The mini Budget came on top of that political change—four

Chancellors, I think, since the summer—and, to a certain extent, in some quarters, some negative commentary on Treasury civil servants. None of that has been helpful, but as someone who came into this after the mini Budget, there has been incredibly impressive service by Treasury civil servants. They are hugely dedicated and professional, and have worked very long hours at times, including weekend working. I pay tribute to the staff who have got through that. In terms of morale, I think that it has had an impact, but staff understand that they are working on really important areas. To a certain extent, the autumn statement has been a very helpful locus to move forward from that and set a more medium-term picture.

Q116 **Chair:** Have you lost any key people? Are you struggling to recruit? Is there anything that you could point to that suggests that that continues to be a problem for you?

James Bowler: No, I wouldn't point to that. We are getting our staff survey, so we will see the numerical effect of how staff are seeing it, and we are going to take that exceptionally seriously. I do not think that we have lost key people. In fact, on the same day that I was appointed permanent secretary, Beth and Cat were appointed permanently as second permanent secretaries. The key capability issue at the moment is an opportunity, which is that we will backfill, if you like, Beth and Cat's posts with two new directors general, which I think will increase our capability at senior levels to make sure that we can look across everything that the Treasury is doing.

A key part of that is looking at the workload of the Treasury and particular pinch points after, as I say, quite a long period of crisis management—for example, people working on energy, which my colleague Phil has been leading on, and people working on Ukraine—making sure that we have long-term solutions to what have been large spikes in work that we did not expect at the start of the year. I would say that, for us three, there are huge economic challenges out there, but we all have a very large focus on staff, staff morale and leadership in the coming period, and we will be looking at the staff survey that is landing as we speak, I think, to give us some strong evidence about where we should be focusing.

Q117 **Chair:** If there is stuff in the results of that survey that you could share with the Committee, we would be very grateful.

I want to move on to the IMF very quickly, Beth, and to ask what the reaction was within the Treasury on 28 September when we started getting commentary from the IMF. We have invited the IMF to come and give evidence to our Committee. So far they have not agreed to give us any evidence on the record, so can you tell us for the record how the Treasury engaged with the IMF when they started making commentary on the UK's fiscal event?

Beth Russell: The IMF are independent and often commentate on what is happening in countries around the world. It was a bit unusual to have that commentary outside a formal engagement with a country. We did not have sight of the statement that they released in advance.

Q118 **Chair:** But when it was made, did you then engage with the IMF? What did the Treasury do to respond to the comments?

Beth Russell: I believe that both the previous Chancellor and the officials on the international side of the Treasury raised it with the fund through the normal channels of engagement. Obviously, we had continuing dialogue, and they also commentated after the autumn statement.

James Bowler: It is worth saying that the annual meetings of the IMF occur every—

Chair: Every year.

James Bowler: In the spring. Work happened in early October. The Chancellor was in Washington and speaking to the IMF and others at those annual meetings and international engagements there. It is probably also worth saying that, in terms of our reaction function, we engaged the IMF on the autumn statement after we had done it and set out what we were doing. The managing director gave, I thought, a very helpful quote about striking the right balance between fiscal responsibility and stability and assisting the most vulnerable—that is a version of the quote; I have it somewhere. So we feel we have been on a journey with the IMF, and that last intervention was really positive.

Q119 **Chair:** Can I encourage you, James, as we are a major shareholder in the IMF, I understand—

James Bowler: Yes, we are.

Chair: —to mention that they ought to be prepared to come and give us on-the-record evidence here.

James Bowler: I am happy to do that. I think they have a policy about engaging with Parliaments. They did talk to the Treasury Select Committee about covid at some point, but I am happy to take that message away.

Q120 **Chair:** Yes, they have given us evidence on the recovery from covid, but we would like to ask them questions about this particular incident because they were so explicit about making commentary on the work of the Treasury, and we feel it is very much in the scope of what we should look at as a Committee. Thank you for that.

Finally, we were hearing, Beth, about the advice you gave to the previous Chancellor on the eve of 23 September about the capacity for the gilt market to absorb the amount of fiscal loosening that was being proposed. What is your view at the moment on the market's appetite for UK gilts? What advice are you giving the current Chancellor?

Beth Russell: The financing requirement for next year is, as I mentioned earlier, pretty unprecedented. That is something that we are keeping a close eye on, but things have stabilised a lot since the autumn statement.

Q121 **Chair:** James, are you in discussions with the Debt Management Office about that?

James Bowler: We certainly are. We set a remit at the autumn statement. Historically our financing requirement is high, so we cannot take that in any way, shape or form for granted. We are in discussions with the Debt Management Office and wider afield. The yields have come back to pre-mini Budget levels, which is encouraging, although not to be taken for granted. That financing requirement—debt stock, debt interest, the path of debt—is a very large part of the work of the Treasury and what we are monitoring and looking at.

Q122 **Chair:** Do you feel, like the previous Governor did, that the UK is dependent on the kindness of strangers?

James Bowler: By definition, yes. Unlike a country like Japan, most of whose debt is bought within its borders, the UK trades its financing requirement internationally, so if you want to borrow—if you want to issue debt—you have to do so on the open market, and that will find the price that people are willing to pay for it. I think that is Mark Carney's quote.

Q123 **Anne Marie Morris:** James, can we move on to spending plans and fiscal rules?

James Bowler: I can certainly do fiscal rules. I might ask Cat Little to help me on spending plans.

Anne Marie Morris: Okay, in which case we will start with the spending plans, Cat. The way the autumn statement set spending out meant that schools and the NHS were going to be well provided for, but departmental spending for other Departments was clearly going to be in a different situation, because they were going to be asked to keep spending at previous levels. Realistically, given where we are, that means that there will have to be some economies—some savings—and some squeeze. Given what you know of current spending trends, where we are with the economy and the pressures we are under with the cost of living, energy and so on, how much of a squeeze do you see being put on those other Departments? Do you think it is going to be evenly spread?

Cat Little: It goes without saying that inflation has had a very big and significant impact on the cash settlements that we provided to Departments at SR21. The OBR estimates that there is a range of between £5.3 billion and £15.3 billion of impact on Departments. That takes into account the additional funding that we provided at the autumn statement, which you mentioned, for health, social care and schools. That represents about 1% to 3% of all public spending, so it is a significant but, we believe, manageable pressure.

I will just talk through a couple of the things we are bearing in mind and some of the actions we are taking to help support Departments in managing the impact of inflation. First, it is important to go back to SR21. At that point, we recognised that there definitely were some indicators of inflation increasing above the levels we have seen before, so we did two things: first, we provided some additional funding for Departments to manage those pressures, and secondly, we created the largest reserves we have had for a very long time in the Treasury. We weren't able to forecast it—I don't think anyone at the time could have predicted quite how significant inflation would be and how fast it would rise—but certainly those two measures are part of the solution.

Secondly, it is important to recognise the downside risk from inflation, but over the course of the last year we have also seen some brakes on spending. In particular, the impact of a narrow labour market and the covid impact on supply chains have actually slowed down our ability to spend, particularly on capital-intensive programmes.

To your point, the impact of inflation falls in very different ways, depending on the nature of the services and activities of each Department. At the autumn statement, we launched the efficiency savings and reprioritisation review, and we are working with all Departments to look at how we can drive efficiency, prioritisation and savings to manage the impact as effectively as we can. We also ask all Departments to put aside a contingency. Every Department every year has to put aside 5% of contingency to manage unforeseen pressures, including inflation. Our hope is that we can work together to counteract some of the most difficult impacts.

The final thing I would say is that there is a very big difference between CPI and the GDP deflator, and that accounts for the range in the OBR's forecasts of the impact that inflation could have. At best, the GDP deflator represents goods and services produced domestically that we think most accurately reflect the sorts of services the public sector produces. At best, we hope that the impact is at the lower end of that range, rather than at the top end of CPI.

Q124 **Anne Marie Morris:** That is very helpful, and the fact that so much has been done already to try to cushion the blow is certainly helpful. Given where we are now, as opposed to when the OBR did its forecast, do you feel it is still the case that that squeeze will be relatively minimal? I think that is what you are saying.

Cat Little: It impacts different Departments in different ways. If I look at our forecast for this first year of the three-year spending review, although the impact and the pressures of inflation and pay have undoubtedly led to Departments making prioritisation and efficiency choices, broadly speaking, with the use of the reserve and the funding made available, we expect to live within the overall spending settlement for this year. Of course, it is unpredictable; we might see inflation for longer than currently predicted, but our hope is that this is a temporary peak. As you know, the OBR currently expects inflation to peak in quarter 2 and then return back to a much more manageable level in due course.

Q125 **Anne Marie Morris:** One of the things that the Chancellor said was that, rather than cutting any major projects, we would look at low-priority and low-value programmes. Do you think that is still achievable? Do you think you can manage to live within the current budgets without cutting any major programmes?

Cat Little: I do. Again, it will be easier for some Departments and harder for others—particularly those Departments that have been impacted by short-term pressures from the pandemic and Ukraine, and where services are highly impacted by inflation. But in the round we are seeing Departments reprioritising without impacting on major priorities, and we have been able to continue to drive efficiency.

Q126 **Anne Marie Morris:** Which Department will be the worst impacted and find this the hardest to achieve?

Cat Little: I would not want to name individual Departments, because we are right in the middle of the efficiency saving and reprioritisation process, which is trying to ascertain exactly how we think inflation and pay will impact. But certainly those Departments that have had more pressures from demand from Ukraine and covid will have more of the pressure, because both demand and inflation have impacted the way in which they provide services.

Q127 **Anne Marie Morris:** It seems to me that Defence and Education are likely to be candidates, but I accept that you—rightly—cannot pick one or the other. Can you give me an example of a low-value, low-priority programme?

Cat Little: I think it would be wrong for me to go into the specifics of those programmes, especially because, as I said, we are right in the middle of this process. It is a political process, and decisions need to be made in the round. Our intention is to ensure that final decisions are made at the spring Budget, so that we can look at the overall position in the round alongside the fiscal event. Just to assure you, our priority is to make sure that we protect public services, the priorities of the Government and the vital services that the country expects us to provide every day.

Q128 **Anne Marie Morris:** If you cannot give me specifics, are you able to explain how you would define something that is a low-value project and something that is low priority? What are the criteria that mean that a particular piece of spending will fall into those categories and therefore be in the list of possible things to be cut?

Cat Little: First, I would point you to the public value framework, which sets out the priority outcomes of Government. At the spending review in 2021, we set out the priority outcomes for Government and the shared outcomes that we expected Government Departments to deliver within their funding settlements. It very explicitly sets out the outcomes, the performance trajectories, and the programmes and projects that were, by default, high priority. Conversely, the sorts of things that we would look at are the things that are not named as high priority in the public value framework. This Government have also been very clear, directly with Departments, about which priorities and manifesto commitments remain priorities, so we expect Departments to take that instruction and make sure that any decisions about prioritisation protect the public commitments that have been made.

Q129 **Anne Marie Morris:** If you find more low-value, low-priority programmes, according to that definition, might you cut more of them rather than choose between them in order to give yourself some headroom?

Cat Little: That clearly will be a choice. We want to make sure that we are not just managing to a bottom line. Ultimately, we need a range, because there is a huge amount of unpredictability. That is why we have the reserve but it is also why we forecast ranges on financial risk as we go through these processes.

I should emphasise that this is not just about changes to programmes; there is a huge amount of work going into driving greater efficiency and productivity in all that we do to drive value for taxpayers' money. We expect quite a lot of the savings to be driven through just better use of public funds and better productivity. My personal view is that greater productivity of our workforce and our assets is something that we all need to focus on.

Q130 **Anne Marie Morris:** Very good; I agree with you. I look forward to learning more about those savings.

Very briefly, James, can I ask you about the fiscal rules and the headroom that we have left? We have £9 billion headroom. I think we all agree that that is quite tight. Against the new fiscal targets, might that be wiped out? If it is wiped out, is there a plan B? Is there a strategy as to what we do if that £9 billion disappears?

James Bowler: The thrust of the whole autumn statement was a balance in how to make sure we supported the economy through recession, while consolidating the public finances and moving together with monetary policy. I think the path that the Chancellor and the Prime Minister have chosen does that.

The fiscal rule that you are quoting is for debt to be falling by the end of the forecast, and there is headroom of £9 billion. A severe change for the worse in the OBR forecasts could mean that goes away. The whole point of fiscal rules is that they guide the actions of the Government and tell people, not least markets, what reaction function they can expect. Were that to happen, the challenge for future Budgets would be to take that forecast and try to get that back on track, and try to continue to live within that fiscal rule.

It has been the case, not least in recent times, with big shocks such as covid and the recent energy shock, that you then might need to recalibrate your fiscal rules and work through, but these are the rules that we have stated and our intention is to live with them. That headroom is not tiny at all—£10 billion is a lot of money—but yes, there absolutely could be situations whereby that is eroded.

Q131 **Anne Marie Morris:** If the economy moves in a way we have not expected and therefore, before we get to the next fiscal event, it is clear that action has to be taken, is there a mechanism, a plan or something you can look to in order to give you a framework to enable you to make a decision, rather than having to wait for the next fiscal event, which, frankly, may not be practical or doable?

James Bowler: The most likely timing for the next fiscal event is spring, which is not too far away—it doesn't feel like that far away in preparing. Absolutely, it would normally be the case that you would look at the forecast that the OBR would give you in time and then set your fiscal stance according to that. There is a set of unusual circumstances—but, let's face it, we've seen quite a bit of unusual circumstances—whereby you might have to make some fiscal interventions between events. Covid and energy are two very good examples of that. You then have the choice as to whether you want to do that outside a fiscal event where you might have to—furlough in covid would be an example of that—or you could try to bring the fiscal event forward, although it is a very large affair and these forecasts, particularly OBR forecasts, cannot be written overnight, as the Committee is aware. But those would be your two choices. At all times, you are going to want to have in mind sustainability and stability, so you would be wary of announcing things without those two watchwords in mind.

Q132 **Anthony Browne:** My questions will be about a dramatically increasing area of public spending: debt interest payments, which are obviously the subject of a lot of public commentary and concern. The OBR report that was just published notes that they double in cash terms from £56.4 billion, or 2.4% of GDP last year, to £120 billion this year. That is 4.8% of GDP, and that is the highest since immediately following the second world war, both as a share of GDP and as a share of revenue. What impact does this have on public spending? Is there a direct correlation—£100 billion extra on interest means that there is £100 billion less for schools and hospitals—or can you refinance in a way that it does not mean that?

James Bowler: The figures you quoted are correct. An increase in debt interest payments is an increase in spending, and there are no magic ways to say that any other way.

Q133 **Anthony Browne:** So that extra £60 billion in interest is £60 billion we cannot spend on public services.

James Bowler: You would struggle to refinance, or to do anything that would have a very immediate short-term impact on that. We are always actively looking at ways of making sure—indeed, it is the remit of the Debt Management Office to make sure—that we are raising that money in the most cost-effective way.

To your question whether it come out of schools and hospitals, the answer is no. We stuck with our departmental spending plans for the coming two years and set a path thereafter. We didn't say, "Those debt interest payments mean that we are going to reopen and cut the allocations elsewhere," but it is a significant driver of our borrowing profile in the coming years.

Q134 **Anthony Browne:** So it makes it more difficult to balance the books or fit within the fiscal rules over the coming years, fundamentally.

James Bowler: Correct. Higher spending makes it more difficult. Our fiscal rules obviously contain the forecasts for debt interest going forward, but it means that borrowing is higher than it otherwise would have been.

Q135 **Anthony Browne:** How worried is the Treasury about the very high level of debt interest payments, and how worried should the public be? A lot of commentators have painted it in fairly apocalyptic terms, although some others have said, "Actually, it's manageable." It is such a huge amount of money.

James Bowler: I would not put it in apocalyptic terms. The main reason I say that is that the UK is not alone in having to go through this. Virtually every other advanced economy is going through something similar: having to repair its public finances, having borrowed and increased debt considerably. The markets know that, and other countries know that.

Where the autumn statement was really interesting—there wasn't as much commentary on it—is that the UK is one of the first countries to set out its path for fiscal consolidation, which is a good thing. The UK is saying to everyone, "This is our reaction function to that." Europe, for example, have still suspended the stability and growth pact, so they have yet to get to that point of how they are going to start to repay that. The obvious point is that the entire focus of the fiscal side of the autumn statement was, indeed, that question, "How are we going to make sure the public finances, including debt interest, are on a sustainable footing?" That is why at the heart of the autumn statement there is a £55 billion consolidation.

Q136 **Anthony Browne:** One of the reasons why the debt interest payments are so high is the large quantity of index-linked gilts in total stock—around a quarter, I think. Obviously, the higher RPI is, the more you have to pay. In the 2018 Budget, you did look at trying to reduce the proportion of index-linked gilts, but is that too little, too late? Isn't it quite a vulnerability to have a quarter of our stock index-linked?

James Bowler: It is not quite as straightforward as that, but you are right. I think it was 28% a few years ago, and we have reduced that to below 20%. It is not quite as easy to say, "Let's not do any index-linked gilts anymore," for several reasons. First, there is a demand and supply and a price in the market. We are selling our debt to a market that demands that debt in different ways, and it demands index-linked gilts. Demand means a lower price, so there is a calculation to be made—

Q137 **Anthony Browne:** But a higher risk if inflation goes up.

James Bowler: Absolutely. The second point is that index-linked gilts tend to be longer in maturity. The UK, by contrast with other countries, has a longer maturity of its debt, which is a good thing, and index-linked gilts tend to be longer. Thirdly, there is a diversification, in that certain people—for example, the pensions industry, through regulatory requirements—demand index-linked protection. There are reasons why your skew—your mix—of the debt you offer is different, which, at the heart of it, comes down to demand and supply. It is not absolutely the case that index-linked is bad and non-index-linked is good—that would be too much of a simplification—but you are right to say we have reduced that in recent years, and we keep that under review. Obviously, it is worth saying that when inflation is high, an index-linked gilt is paying more, but these gilts go over a number of years.

Q138 **Anthony Browne:** Do you think it was a mistake to allow the stock of index-linked gilts to rise to nearly 30%, which is very high? It is high risk: if inflation does rise, you have a double whammy of rising interest rates and rising inflation.

James Bowler: For the reasons I set out, I don't think it was a mistake, but it is definitely something to keep under review. You need to have an understanding of what you think your inflation expectations are going to be over the period, and you need to mix demand, price and diversification as you set that forward.

Q139 **Anthony Browne:** Do you think the current level of gilt issuance is the right amount?

James Bowler: We set a remit every fiscal event and we are going to keep that under review, but as I said, it is mainly determined by demand and supply as well as other factors. To a certain extent, the negative aspect of the gilt would be its openness to inflation, but you might pay a cheaper price, so it is a calculation. It is difficult to say exactly whether it is right or wrong, but we have reduced the stock. I think it was 28% in 2019, and now it is more like 22%. We will keep that under review, with a view to making sure that we are always borrowing at the most effective cost to the taxpayer.

Q140 **Anthony Browne:** You mentioned the maturity of the debt, which is historically quite long compared with other countries. It has come down a lot as a result of quantitative easing, I understand, but it has gone from over seven years to about two years. Obviously, that makes us a lot more vulnerable to short-term changes in interest rates—they have an impact a lot more quickly. There are lots of arguments for and against quantitative easing, and I do not expect you to go through that now, but it has meant we are more quickly hit by a rise in interest rates than we would otherwise have been.

James Bowler: I think the OBR did a box or a feature on that in their report. Yes, it is the case that quantitative easing is swapping long-term for shorter-term things, which has the impact of reducing that maturity. It is still the case that we are in a longer place than everyone else, but the reality is that that quantitative easing has happened, and we are now left with the stock of over £800 billion of quantitative easing. Actually, we are now into a quantitative-tightening cycle, so that is now being decided on—as part of monetary policy—by the Monetary Policy Committee as to how they do that.

The reaction function cannot be to say, "I wish we hadn't done all that quantitative easing," because it's there. I think the reaction function is the right one, which is that we are consolidating the public finances and the Monetary Policy Committee—the Bank of England—are taking decisions on the size of QE or the size of quantitative tightening as part of monetary policy, which obviously has an impact on the interest rate decisions they take, too.

Q141 **Anthony Browne:** Finally, there has been some media commentary—partly speculation by some former Bank of England officials—that the Government could reduce the interest costs associated with the asset purchase facility by not paying so much interest on all the reserves that commercial banks have. Huw Pill, the chief economist at the Bank, had said that that would not be the right thing to do; I think somebody else said that it is a form of default. I just wondered what the Treasury position would be on this.

James Bowler: There would be no plans to do that.

Q142 **Anthony Browne:** You have not considered it at all?

James Bowler: No.

Q143 **Dame Angela Eagle:** Mr Bowler, what input on splitting the fiscal events into growth and then spending later did you have? Did you warn the then Chancellor and Prime Minister that this was not a coherent way to behave?

James Bowler: I am using my understanding from arriving after the event, but I am absolutely satisfied that Treasury officials set out the right advice to the then Chancellor. That included setting out how we would usually go about linking any large fiscal event with an OBR forecast concurrently.

I think it's probably worth saying as we look back, in addition to the answers that the second permanent secretaries gave, that I think many of the decisions here were taken in the leadership contest for the Conservative party. I think that when it came to it, many of those decisions on how to proceed in terms of the policies—the majority of the policies themselves and then how they wanted to announce those policies—were taken before the Prime Minister became Prime Minister and the Chancellor became Chancellor.

Q144 **Dame Angela Eagle:** So were they impervious to the advice that was offered?

James Bowler: Well, officials advise and Ministers decide.

Q145 **Dame Angela Eagle:** Do you think that we need to learn any lessons, particularly about perhaps allowing the OBR the independence to publish when there is a fiscal event in future so they cannot actually be blocked from publishing a forecast, because everyone else published forecasts anyway and it merely made the entire thing look illegitimate and shady?

James Bowler: Certainly, one of the major lessons learned from the whole situation was to avoid splitting a major fiscal event from a forecast. Indeed, it's worth saying that, if you like, the giveaways were in the growth plan and the consolidation was going to come later in the medium-term fiscal plan. To do the giveaways, the forecast and the medium-term plan separately wasn't sensible. I think it is indeed the case that you would want in the future—in normal times—always to combine any large fiscal event with a forecast. I've got no problem suggesting that that is a clear lesson learned.

The one thing that I would say is that, of course, we have just been through some fairly extraordinary times, in terms of covid, and where you were doing—

Q146 **Dame Angela Eagle:** Yes, but with all due respect, that was prior to this particular episode.

James Bowler: I was just making the point that if you were looking forward to write how you would do that, you'd want to bear that kind of situation in mind—

Q147 **Dame Angela Eagle:** I mean, covid was an exogenous shock and this was a self-inflicted catastrophe, wasn't it?

James Bowler: Your words.

Q148 **Dame Angela Eagle:** Hmm. What role has the Treasury played in the bail-out of Bulb Energy?

James Bowler: I'll ask my colleague Phil Duffy to answer that, as he knows considerably more about it than I do.

Phil Duffy: We have been involved with the Bulb M&A and administration since we first heard about the difficulties they were facing. As it is a lead for our colleagues in BEIS, our role has been to ensure that there was adequate finance available—emergency finance, in this case—for Bulb to maintain operations, and we have been tracking that right the way through, although the decisions formally sit with our colleagues in BEIS.

I would say two things about that. First, there have been lots of costs bandied around. I have seen dozens of numbers around this—

Q149 **Dame Angela Eagle:** The costs bandied around are in the OBR report. It's £6.5 billion—

Phil Duffy: Well, that is one of the costs.

Dame Angela Eagle Making it the largest bail-out of a private-sector company since one of the banks.

Phil Duffy: Let me address that directly. That number is a gross cash requirement estimate for the total working capital required to not only maintain Bulb's operations, but purchase gas for the 1.5 million people who rely on Bulb to provide gas this winter. What it is not—

Dame Angela Eagle: And the Government are not allowed to hedge, are they?

Phil Duffy: I will come on to that in a second. First of all, we have to be very careful with that number you have just quoted from the OBR, because that number is just the gross outflow. It doesn't take into account the expectation that people who buy their gas from Bulb will pay for that gas now and next year, and also that, if there is any shortfall, the way the legislation operates for the special administration regime provides that that money can be successfully recouped. Overall, our expectation is that the Bulb process will be fiscally neutral—

Q150 **Dame Angela Eagle:** It said in the letter published today that that would be the case, but over how many years?

Phil Duffy: The honest answer is that we haven't decided. We have some decisions to take about the profile of the repayments we want to make on that. It is a perfectly legitimate use of the public balance sheet to smooth those costs over a period of time. With the way the legislation operates, the Business Secretary will have options as to over how many years they wish to recoup the costs of the Bulb administration. When they have done that, we will notify the OBR, which will then issue an updated set of costs at the next forecast that reflect that repayment profile over the years to come.

Q151 **Dame Angela Eagle:** Are these costs likely to appear on customers' bills?

Phil Duffy: They may do. The majority of them—

Dame Angela Eagle: At £6.5 billion, for example, that is £200 per household.

Phil Duffy: Let's just reassure people listening to this inquiry that that is not going to happen, because the majority of those costs will be for the purchase of gas for the 1.5 million Bulb customers. That gas will be paid for by those customers, who are, by the way, generally slightly wealthier than the normal profile of gas users across the UK. If there is any residual at the end of that process, and there may be—for example, we have costs to pay for the administrator, Teneo—then, at that point, we will consider whether we want to recoup that from users of the gas system as a whole. That is how the legislation operates. BEIS will follow that legislation when they get to that moment.

Q152 **Dame Angela Eagle:** This is a catastrophic failure of regulation by Ofgem, isn't it? Some 29 companies have gone bust. A range of people who set up companies waltzed off with vast profits themselves, leaving public liabilities to go on people's energy bills. You can't be happy in the Treasury with the state of regulation of the energy market.

Phil Duffy: I think we would accept quite a lot of what you have just said. We had a number of uncapitalised energy traders, who didn't have to hedge their requirements in advance and then got caught out when the prices rocketed following the invasion of Ukraine. The good news is that we are working very closely with Ofgem and BEIS on changing that regulatory model. As we speak, energy for the next six months and beyond, into next year, is fully hedged. That is a very important requirement. I know that colleagues in Ofgem are looking at, for example, introducing capitalisation requirements on market participants—

Dame Angela Eagle: What is known as closing the stable door after the horse has bolted, I think.

Phil Duffy: That is a very fair comment, but we are now fixing this problem.

Q153 **Dame Angela Eagle:** This morning and over the weekend, the Prime Minister said that funding public pay claims would cost £1,000 per household. James Bowler, do you agree with that figure?

James Bowler: I did see that over the weekend. I don't know whether that figure emanates from anyone in the Treasury, so I am not aware of the calculation of it.

Q154 **Dame Angela Eagle:** The Prime Minister said it would cost an extra £1,000 per household. There are lots of things wrong with that, given that it is the entire cost if no tax is paid and no other companies pay tax on the increases. How do you feel about the Prime Minister and then half the Cabinet using these kinds of figures, which are clearly not correct and are actively misleading?

James Bowler: I guess there are established procedures under statistics watchdogs, which set out whether they feel that politicians are using sensible figures.

Q155 **Dame Angela Eagle:** They are Cabinet Ministers. Don't blame all politicians for this. They are Cabinet Ministers who ought to know better, from the Prime Minister down.

James Bowler: In fairness, the statistics people look at whether things are being misquoted on both sides of the House. Clearly, the Prime Minister is making a calculation based on the difference between existing pay settlements and very high levels of inflation. This country and others—all the G7 countries—are seeing real household disposable income falling because levels of pay are less than levels of inflation at the moment.

Q156 **Dame Angela Eagle:** But do you think it is fair to say that increasing public sector pay by inflation would cost £28 billion, on top of amounts already budgeted for within departmental settlements?

James Bowler: I'm afraid I don't have the calculations in front of me.

Q157 **Dame Angela Eagle:** Could you write to us with them? You are the people who look after the departmental settlements, so could you write to us?

James Bowler: Yes, I can take that away. I think my colleague is wanting to come in.

Q158 **Dame Angela Eagle:** Cat, do you want to answer? Have you got these figures at the tip of your tongue?

Cat Little: I do recognise the calculation. It basically takes the pay bill expected based on SR settlements for next year, and multiplies it by CPI this year. It is the gross calculation; it doesn't take into account current funding available for pay. That is where the £28 billion derives from—it is 11.1% multiplied by the expected pay bill.

Q159 **Dame Angela Eagle:** So it is not accurate then, is it?

Cat Little: I think it is accurate in so far as—

Q160 **Dame Angela Eagle:** It would only be accurate if the Treasury had budgeted for a zero pay increase this year. The £28 billion would be for the entire cost of the pay bill increase.

Cat Little: My understanding of the way in which the calculation has been drawn is that it is—

Q161 **Dame Angela Eagle:** You budgeted for 3% or 4%. In the financial settlements that the Treasury agreed, there was a pay rise agreed, wasn't there? It wasn't 11%, but some potential public sector pay rises were taken into account.

Cat Little: Absolutely. When we set the spending review assumptions about pay, we make an assumption. That is very difficult to do in the middle of increasing inflation, as I implied earlier. A year ago, we set an assumption about pay for this year and for all the years included in the autumn statement and the spending review. This year, pay deals have been concluded and they have been absorbed within spending settlements with Departments. The expectation is that any increases to pay will be absorbed from existing departmental cash settlements. That is standard practice, and always has been.

Q162 **Dame Angela Eagle:** Yes, but you are not answering my question. The £28 billion cost is not an accurate summary of what would happen if pay claims were to be exceeded. You have already budgeted for some increases, as you have just said, so that takes money off the £28 billion.

Cat Little: Yes. As I said, the figure that you quoted is gross, and it does not take into account the net settlements already provided.

Q163 **Dame Angela Eagle:** So that £1,000 per household figure is wrong and misleading, isn't it?

Cat Little: I don't know how that figure has been specifically used in lots of ways, but I recognise that it is an inferred calculation from—as I described—inflation applied to a pay bill and then translated into what that would mean for individual households.

Q164 **Chair:** Could you follow up on that and let the Committee know? Clearly the amount is not zero. The £1,000 is a round number that has obviously been a subject of debate here. It would be helpful if Treasury brains could come up with the number, which is not zero.

Cat Little: Of course.

Q165 **Dame Andrea Leadsom:** Good afternoon. Mr Bowler, you said earlier to my colleague Anne Marie Morris that you look at productivity and value for taxpayer money across Whitehall. Have you looked at the impact on productivity and value for money as a result of the civil service working from home across Whitehall, particularly in areas like driving licences, the Passport Office and perhaps even the Treasury?

James Bowler: I am not aware that we have done that study explicitly. As my colleague Cat Little set out earlier, we have very significant reviews under way for efficiency in terms of savings and lower-priority spending and also productivity—public sector productivity is in that—but I am not alive to calculations going right down to the specifics.

Q166 **Dame Andrea Leadsom:** Okay. It would be very helpful to know. You mentioned earlier that the civil service has come under some criticism, which you consider unfair, but there is a concern, particularly in constituency mailbags, about the impossibility of getting a driver's licence, passport renewal and so on. Right across Whitehall, productivity has been impacted by working from home, so it would be helpful if you could look into that specifically.

Moving on, in response to questions from my colleague Dame Angela Eagle you mentioned that there is a review of the regulation of energy companies. Is it the thinking that they may be required to have capital in the same way that banks do? Is that where the direction of travel is?

Phil Duffy: You should probably direct that question to Ofgem, which is doing the review. My understanding is that at the minute there is no capitalisation requirement. We think there is a degree of capital they need to have so that they can post counterparty risk for purchasing their gas supply. The combination of the thinking about their capitalisation requirement and their obligations to forward-purchase gas is intended to avoid this problem. Currently, they have to purchase the gas they need for their customers six months out. That is a new measure. My understanding is that Ofgem will be setting out shortly its thoughts on the level of capitalisation required and what would be an appropriate level.

Q167 **Dame Andrea Leadsom:** But they will therefore be marking their own homework, won't they?

Phil Duffy: Ofgem will be bearing in mind that a very high level of capitalisation would impose significant costs on energy bill payers, because capital has a cost to it.

Q168 **Dame Andrea Leadsom:** Yes, but so do massive failures. This is a broken system, isn't it? Will the Treasury be involved in providing advice to Ofgem, which has clearly failed to regulate successfully? Will you be providing advice? Would your advice be to regulate them like banks, requiring capital?

Phil Duffy: First, we work very closely will Ofgem, which I think has had an incredibly challenging year responding to these problems, so I feel it deserves some credit for the response it has launched. When you say bank-like, I do not quite know what that would mean—

Q169 **Dame Andrea Leadsom:** Well, requiring capital so that in the event of a rise in energy prices, companies do not go bust.

Phil Duffy: We are looking at whether there is a requirement for a level of capitalisation that was absent from some of the very thinly capitalised companies that entered the market. All that said, we have effectively forced a level of capitalisation, because currently you have to buy in advance your gas supply. That has already been taken into account.

James Bowler: It is worth saying when we are answering these questions that Ofgem is an arm's length body of BEIS. The Treasury has an overarching view on all these issues, including wanting efficiency and anything that is going to be a challenge, such as growth in the economy. As Phil is answering your questions, he is doing that through several steps removed.

Q170 **Dame Andrea Leadsom:** I fully appreciate that, but, having been a Minister in the Treasury and BEIS, I know very well how it works. Unfortunately, this has fallen through the gaps. This is a massive failure. It is costing people a fortune at a time when energy prices have already absolutely rocketed.

What I am asking for is your view on how you are going to force Ofgem to fix this. Again, perhaps that is something that will evolve over time, but I do not think it is a complicated question. Will you require capital like banks have to have? In other words, in the event that they have losses due to their own trading—which might be buying forward financial instruments, not oil, but nevertheless—the banks are required to keep capital against their own losses, and at the moment energy companies are not. Is that something the Treasury might require them to do?

Phil Duffy: That is a proposal that is being actively considered by Ofgem. Just to reassure you, we talk all the time to Ofgem and BEIS about the situation. There isn't any gap between us. We want a resilient, well-regulated sector and we recognise that there have been very significant regulatory failings in the last few years.

Q171 **Dame Andrea Leadsom:** Good—thank you. Moving on, in the OBR's forecast, it has anticipated a 12p increase in fuel duty from next April. That is quite significant at a time when, evidently, wholesale prices are coming down but prices at pumps are not. What is the Treasury's view on forecasting for something that has not happened in the last 12 years? Is that sensible forecasting policy? What do you do about the £6 billion black hole that creates in the event that fuel duty is frozen again?

James Bowler: I will ask my colleague Beth Russell to come in on that.

Beth Russell: Basically, the forecast is done in this way traditionally. It is a long-standing assumption that fuel duty increases by the rate of inflation and that is then only changed when the Government make a decision about what the policy will be, which, as the Chancellor said, has not yet been taken for next spring. Obviously, we as Treasury officials will be advising on the issues around that, including the costs and the wider economic and other impacts. We will look at how to fund the cost of that alongside other measures in the next—

Q172 **Dame Andrea Leadsom:** Yes, Ms Russell, I completely understand that—I totally understand that there are choices, that these are political choices and that the Treasury Ministers have not decided yet—but does it not make a nonsense of forecasting? In effect, you have £6 billion in there that you may or may not have. The last 12 years suggest you will not have it. Therefore, does it not make a mockery of the forecast?

Beth Russell: Well, it is the approach taken across taxes.

Dame Andrea Leadsom: But you have a 12-year track record.

Beth Russell: Yes and, as you say, fuel duty has been in a particular position. Obviously, it would be a ministerial decision to change that assumption for the longer term and there would be a permanent cost to doing that at a time that they decided to do it. That is not the position at the moment. The position is that the default is an RPI increase.

Q173 **Dame Andrea Leadsom:** I would assert that it makes a mockery of forecasting.

James Bowler: You make a reasonable point, and I think that is why the Chancellor has been on the record saying what his expectations are. There are swings and roundabouts in the whole system. I will take some of your examples. On fuel duty, there is an expectation that it will be index linked the next year. On the conversation we are having about energy, there is nothing in the forecast that suggests some of the funding will come back to the taxpayer, and that is because the OBR in particular just takes the policy that they have in front of them on the day and will not speculate about future policy. I am not blaming the OBR for that.

Dame Andrea Leadsom: No, understood—they can only do what is in front of them.

James Bowler: They can only do what is in front of them.

Q174 **Dame Andrea Leadsom:** Nevertheless, the question remains: is that a good way to go about forecasting?

James Bowler: I think that is a reasonable point.

Dame Andrea Leadsom: Would it not be better to have a review of this and make a balanced decision? Maybe you could show two figures—one with and one without. You will have been aware of the huge furore about the expectation that was in that forecast for fuel duty. The Chancellor had to write to us to make it very clear that was simply a non-decision as yet, but it is very misleading. Anyway, I will leave it there.

It has been reported that several large offshore oil and gas firms are planning to reduce their investment in North sea projects in response to the increase in the energy windfall tax. Are you concerned about this? Have you made allowances for that in terms of forecasting for future investment?

Beth Russell: Obviously, it is reasonably early days with this, and we are carefully monitoring what is happening. There is lots of dialogue with the industry. Indeed, the Chancellor met representatives of the industry on Friday. What Ministers have been trying to do with this policy is get the balance right between taxing extraordinary returns—taxing the windfalls—while still maintaining incentives for investment. That is why there is a generous investment allowance in the tax. The OBR said that it does not expect there to be an impact on investment from the two windfall taxes, but we are not being complacent—we are monitoring it, keeping it under review and talking to the industry.

Q175 **Dame Andrea Leadsom:** So you are talking to the industry about its plans.

Beth Russell: Yes.

Q176 **Dame Andrea Leadsom:** What would you say is the reaction in terms of investment intentions?

Beth Russell: Obviously it is a new tax, and industry does not necessarily react favourably to that. As I say, our existing assessment of the impact on investment is that it is not going to be significant, but we will keep talking and looking at what actually happens.

Q177 **Dame Andrea Leadsom:** Thank you. Moving on to the FSMA Bill, what was it, Mr Bowler, that led to the eventual dropping of the proposed intervention or call-in power for the Treasury?

James Bowler: I think Ministers took the view that the powers in the Bill were sufficient. The Bill is a very significant move to devolve regulation to our regulators, having come out of the European Union. I think Ministers took the view that the number of checks and balances and accountabilities in the Bill—including the opportunity for the Government to instruct the Treasury to review a rule if it so wishes—were sufficient. But the Government did say they will keep that under review.

Q178 **Dame Andrea Leadsom:** They also gave themselves some amendments that would enable the Treasury to require the regulators to publish information on requested matters at any time. Is that an alternative?

James Bowler: No, I do not think that is an alternative to what was going to be the intervention power. The intervention power was going to be used in exceptional circumstances to intervene. I think the amendments of the last week are for the regulators to publish performance data—for example, on how quickly they are doing the things they are doing, and for them to be more transparent as we set up this regime.

Q179 **Dame Andrea Leadsom:** Thank you. On Solvency II, what potential do we think it has for increasing London's competitiveness? Do we think that could be very attractive for UK PLC?

James Bowler: Yes, I hope it is attractive. The main driver in the balance we struck in Solvency II was to allow firms to be able to invest in slightly more liquid assets, such as infrastructure assets, which are going to be key to net zero. In terms of giving you a number, the industry itself has talked about that loosening up £100 billion of investment.

Q180 **Dame Andrea Leadsom:** Do you think that will come to the UK?

James Bowler: Yes. They are talking about that being the investment for the UK. It is very much worth stressing that this was done in conjunction with carefully plotting what the regulatory regime would be going forward, which includes a mixture of a rules-based approach and the supervisory approach of the PRA.

Q181 **Dame Andrea Leadsom:** So do you anticipate more money invested in UK infrastructure projects? Is that the ambition?

James Bowler: Yes. I think the industry itself has said that it expects this to unlock more than £100 billion for investment in long-term productive assets.

Q182 **Dame Andrea Leadsom:** This is the final question from me. Ringfencing was a key post-financial crisis reform, and it was brought in only in around 2014-15. Why has the Treasury got such a short memory?

James Bowler: This is really important. Ringfencing remains—continues—and the announcements made on Friday do not get rid of ringfencing. The announcements set out on Friday were part of a measured and evidence-based approach informed by a review by Keith Skeoch that talks about addressing some of the unintended consequences of the original approach and some of the scope. The changes are to both and they have been welcomed by industry and regulators alike, but they do not end ringfencing.

Q183 **Dame Andrea Leadsom:** But does it risk a sort of two-tier system in which smaller businesses can get away with it and bigger businesses cannot?

James Bowler: I do not think the changes announced on Friday do that. The changes announced on Friday are about two things. First, they are about representing the fact that things move on and recognising where we are, but, as I said, that was done on and in conjunction with a very careful evidence base. Secondly, they are also part of a very large body of work, which the Treasury is at the heart of, to move regulation that had been done at a European level into the UK. We are going to do that, essentially, through our independent regulating strategy. That is the focus of those—it is not about trying to differentiate.

Q184 **Dame Andrea Leadsom:** Ringfencing was a UK invention, not an EU invention.

James Bowler: Yes, ringfencing was UK.

Dame Andrea Leadsom: So it is not part of a post-Brexit change.

James Bowler: No.

Q185 **Dame Andrea Leadsom:** It is a case of our having decided that we got it wrong or that it was too tight. Is it a pro-competitiveness measure? If so, does it also increase financial stability risks?

James Bowler: If anything, some of the changes are about competition to benefit consumers rather than the whole size of things—we increased the retail deposit threshold to allow more competition for consumers—but the focus of the wider change in ringfencing was essentially to look at addressing some of the unintended consequences of the former regime. For example, it is about allowing banks to provide more corporate services and support financial advisers where they could not do that before. As I said—you make a very good point about the lessons from the past and the very large consequences—we have done this incredibly carefully, informed by independent reviews and the evidence base, and the ringfencing remains very much in place.

Chair: Thank you very much. I am sure that will be something that the Committee will be scrutinising further as the consultations and so on progress, including by taking evidence from Skeoch and Vickers, I would imagine.

Q186 **Rushanara Ali:** I have some further questions on the mini Budget and then some on PPE contracts. Let me start with Beth Russell and Cat Little, as you were in post during the mini Budget. Did Treasury officials give advice to the then Chancellor about the potential impact of the mini Budget on financial markets? You mentioned that some advice was given; could you say a bit more about the nature of that advice? Did the market reaction come as a surprise to officials, including yourselves?

Beth Russell: I will come in and then Cat may want to contribute as well. I do not think we should get into a blow-by-blow account of the exact advice that we gave to Ministers—obviously that is confidential—but, as I said earlier, people gave advice on—

Rushanara Ali: Well, I think it would be helpful for taxpayers to know, because there have been serious detrimental effects, so we do need to know the answers to those questions, please.

Beth Russell: As I said earlier, we gave advice on the cost of measures in the normal way—the economic and fiscal backdrop and the economic and fiscal impacts of measures. We gave advice on the consequences for the financing requirement and we gave advice on what was happening in the market and the market expectations for the effect.

Q187 **Rushanara Ali:** So you explained the market reaction to Ministers—or did that come as a surprise to you when the mini-Budget was announced?

Beth Russell: I think it is fair to say that we knew that there were risks and it was something that we heightened our monitoring around, particularly because of the impact of the increase in the financing requirement.

Q188 **Rushanara Ali:** Did you explain what the risks were to Ministers when you were giving advice?

Beth Russell: Yes, I am confident that we did and all the risks that we should have done in our—

Q189 **Rushanara Ali:** Can you shed a light on what precisely you were setting out in terms of risks in market reaction?

Beth Russell: As I said, there was the risk of the fact that the financing requirement was going to be much, much higher as a result of this event, and then the risk around market expectations and the potential mismatch between the size of the intervention and what was expected by the market.

Q190 **Rushanara Ali:** Did you provide any numbers in terms of what the cost would be and what the fall out would be, if Ministers pursued the course of action that they were pursuing?

Beth Russell: We obviously provided advice on the cost of the measures. In terms of the market reaction, that is a very difficult thing to predict, and I do not think we could have advised on exactly what that would be, but we advised on the fact that there was a risk.

Q191 **Rushanara Ali:** But you did raise the alarm bells? You are saying that you did point out the risks and you did raise the alarm bells.

Beth Russell: We did, yes.

Q192 **Rushanara Ali:** And what was the reaction of Ministers when you raised the alarm bells in advance of the mini Budget announcement?

Beth Russell: As James said earlier, it is for us to advise and Ministers to decide—

Q193 **Rushanara Ali:** So they basically said they were going to ignore you. The euphemism of what you are saying is they basically said, "No. We're going to go ahead", and ignored you.

Beth Russell: Those are your words rather than mine, but we provided all the advice that I think we should have provided.

Q194 **Rushanara Ali:** Thank you. Following the autumn statement, Richard Hughes from the OBR told us that fiscal decisions need to be "informed by an up-to-date view of the economic outlook." Is that the Treasury's view as well?

James Bowler: Yes.

Beth Russell: Do you want me to answer that again? As James said earlier, we always advise that any significant fiscal interventions should, ideally, be accompanied by a forecast. As James said, that is not always possible as we have to operate at speed—there were particular reasons for that during covid, obviously—but in this instance, we advised on the benefit of doing a forecast. The issue is with moving away from that, but ultimately that is a decision for Ministers to take.

Q195 **Rushanara Ali:** Richard Hughes also pointed other instances, such as the health and social care levy and, of course, the mini Budget. We all recognise that in emergencies, such as covid, there can be exceptions made. Do you think it is good practice for the Treasury to accompany any announcements of significant fiscal measures, such as those, with an OBR forecast?

Beth Russell: As James said earlier, I think that is right, where possible.

James Bowler: That is what we would usually advise, yes.

Q196 **Rushanara Ali:** Okay. Do you think anything should be done to stop Ministers getting into the habit of renaming things so that they do not have to provide independent forecasts or find other excuses, as we have seen in recent times, leaving aside covid and other major crises?

James Bowler: Yes. I think the absolutely clear lessons from past events, and I am happy to state it, were that you do not want to separate the loosening from the forecast and from the consolidation. I am very happy to state that those things are best done together.

Q197 **Rushanara Ali:** Thank you, James. In his evidence to the Lords Economic Affairs Committee, the Governor of the Bank of England noted that Treasury officials, as is usual, briefed the MPC at its meeting of the Government's position and the upcoming growth plan. The Governor said, "I do not think that Treasury officials were clear on what was going to be in it at that point." What did the Treasury officials know? That seems quite different from what you were talking about earlier, Beth. Was the briefing different to other briefings that have been given to previous MPC meetings at similar times? It would be helpful if you can clarify.

James Bowler: Let me try to do just that. As the Governor said, the Treasury representative attended the MPC meetings as per usual but, pertinent to your last question, what was different was there was no OBR forecast. It is worth saying that that has a number of implications. First, you cannot see what is happening in context, so you do not see it with the wider forecast of both the economic and the fiscal position, and you cannot see the OBR's views of the impact of your measures on the economy.

The second side of it, which I think is what the Governor was referring to, is that when you do an event with the OBR, you have to decide your major measures relatively sooner. You have to shut them down sometimes over a week before the event. Those meetings of the embassy happened over a period of time. In a normal run of affairs, if you were having these two events so close to each other, the Treasury official would be able to say with certainty quite a bit before the fiscal event what Ministers have and have not decided, and that was not the case here.

Q198 **Rushanara Ali:** This particular official who speaks to the MPC was not able to brief the Bank appropriately, given what you are saying. Beth Russell and colleagues were giving advice to Ministers setting out some of the concerns. There is the quote "officials advise, Ministers decide", and

Ministers obviously decided—these are my words—to ignore that advice. That did not feed into the Governor of the Bank of England either. Is that right? Am I understanding this correctly? The advice that Ministers received, with alarm bells being raised by Beth Russell and others, went to Ministers, but the Bank did not receive that information.

James Bowler: There were lots of different things going on.

Q199 **Rushanara Ali:** Sure, but that actually would have been quite helpful for the Bank to know about, but that is not what happened.

The growth plan saw the publication of table 4.3 on the "Illustrative effects on tax receipts of"—hypothetical—"higher GDP". Who asked for this table, and was this apparently technical table there for purely political purposes? Perhaps, again, those officials who were there at the time could answer that.

Beth Russell: I am not quite sure which table you are referring to, so it might be something that we need to come back on.

Rushanara Ali: It is in the growth plan—table 4.3.

Q200 **Chair:** It is the one that shows the beneficial impact on tax receipts of growth hypothetically.

Rushanara Ali: "Illustrative effects on tax receipts of higher GDP growth". It is in the growth plan—

James Bowler: I don't know exactly what the table is either, but it is probably worth saying that—

Q201 **Rushanara Ali:** Well, the table was produced by your Department, with respect. The least the Committee expects is that, before turning up to the Committee, officials read the documents and know of a table that is highly sensitive and seems to be purely political, so you are able to understand what that question is about.

James Bowler: Sorry, I was trying to be helpful. Certainly, I was going to try to help on that—

Q202 **Rushanara Ali:** Do you want to try to answer that, please?

James Bowler: The growth forecast used in a fiscal event, like we just had in the autumn statement, has to go off the OBR's growth forecast.

Q203 **Rushanara Ali:** But there was no OBR forecast, so could somebody please try to answer this question? If you do not, could you write to us? What we are trying to establish is whether the Treasury was being leaned on to produce something that looked technical, but was actually purely political, and which had major ramifications on our economy and our citizens. We need to understand that your independence and objectivity is not compromised going forward, because it is hugely damaging for our economy and, for that matter, our politics. Is that something you can write to us about?

James Bowler: Certainly, yes.

Q204 **Rushanara Ali:** Thank you. Turning to PPE contracts, was the fast-track programming in PPE equipment, where cross-Government PPE teams established a high-priority lane to process potential leads referred to them by Government officials, Ministers, officers, MPs, Lords and senior NHS staff, a mistake with the benefit of hindsight?

James Bowler: I am going to ask my colleague Cat Little to answer that question, because she is well versed in it and I think she can set out what the Treasury's role was and wasn't in that example.

Q205 **Rushanara Ali:** Just to recap, Cat Little, you responded to some of the questions that I raised in December 2021. In September 2020, I raised PPE contracts with the then Prime Minister, Boris Johnson, and some of the political dimensions to them. In that session in 2021, you set out that you were aware of the way the Department of Health and Social Care had issued contracts. In the light of what has recently been exposed, including the Baroness Mone case, can you tell us whether, with the benefit of hindsight, this approach was a mistake?

Cat Little: I do not want to repeat the conversation we had in the past, for obvious reasons—for efficiency of time. I emphasise that our role on PPE was, first, to ensure that funding was in place. We took a very early decision, which was that we needed to make sure the funding was available, because we felt that any delays would have increased the risk of PPE not being available on the frontline. The risks associated with providing a very generous material envelope to the Department of Health and Social Care were outweighed by the risks to public health.

It was a very exceptional, unique thing for the Treasury to do in the first place, which is why we put in place quite a lot of additional arrangements and conditions. As I said to this Committee last December, I was never made aware of the high priority lane. What I can say is that—

Q206 **Rushanara Ali:** Sorry, could you repeat that?

Cat Little: I was not personally aware, as I said to you last year, of this being a procurement route or an accelerated procurement route. Once the Treasury provides funding, it is over to the Departments to make sure they are complying with managing public money and good commercial practice.

We have had a number of reviews into PPE and the commercial practices undertaken. We had an NAO report, which went to the PAC earlier this year, and the Boardman review, led independently by Nigel Boardman as part of the Cabinet Office. There are a number of big lessons learned, which I know the Government has accepted and the Department of Health and Social Care is following through on. There are definitely lessons learned in the way in which the high priority lane was applied.

Q207 **Rushanara Ali:** Are there any specific additional lessons for the Treasury to learn from the PPE contracts initiated by Baroness Mone to the company PPE Medpro?

Cat Little: Not on that specific contract. As I said to you before, there are several other lessons learned that we have worked very closely with the Department of Health and Social Care and the Cabinet Office on. There are four that we have most closely been involved in. First, we are making sure we have an integrated stock management system within the Department of Health and Social Care that talks to its general ledger. That was not the case at the time that the increase in PPE purchasing was started.

We also learned that the spending control framework is incredibly flexible, but you need to put in place further checks and balances when we provide additional delegations to Departments. We also learned that the integration of complex commercial specialists into the design of procurement processes right up front is critical. We learned that across quite a lot of the procurement that was undertaken during covid.

Q208 **Mr Baron:** Can I turn to financial sanctions, and specifically the work of the Office of Financial Sanctions Implementation? We would like to know how OFSI is getting on since the Committee took evidence in June. Specifically, is it managing to expand its permanent staffing to adapt to the Russian sanctions regime?

Secondly, as a bit of a drill-down on that, we understand from the annual review that OFSI is experiencing high application volumes for licensing. What are your average response times for high and lower priority cases?

James Bowler: I'm going to ask my colleague Cat Little to come in on that, but suffice to say that OFSI is expanding and has done an absolutely incredible job over the last however many months since the invasion of Ukraine. Cat, could you come in with a detailed answer?

Cat Little: OFSI has performed a remarkable role. It has doubled in size over the course of the last year. It has gone from around 50 full-time members of staff to about 100. It is now dealing with over 1,200 designations and around £80 billion-worth of frozen assets. We have also, following the oil price cap policy announcement last week, set up a dedicated team within the Treasury who will be monitoring the oil price cap. We keep it under very close review, to make sure that we have the capacity and the expertise to be able to fulfil this vital role. I am afraid that I do not have to hand the very specific detail that you have requested on licensing, but I can certainly write to you to make sure that we can set that out for you.

Q209 **Mr Baron:** Thank you. Can I press you a little bit, though? That sounds like an impressive increase in numbers and resource, but is it sufficient to deal with the task at hand?

Cat Little: Our view is yes, it is sufficient. We have worked very hard to be able to demonstrate what we think is good value for money in terms of the numbers of people we are employing but also the skills and the capability that we think we need. This is very specialist, painstaking work, and we ask our teams to work around the clock on quite a lot of the activity that they undertake. At the moment, yes, and, as I say, we will keep it under very close review.

Q210 **Mr Baron:** Thank you. The Economic Crime (Transparency and Enforcement) Act 2022 intended to streamline parts of OFSI's work. The Treasury has had these powers for nearly nine months. Has this changed the Treasury's approach to sanctions in any way? For example, are you seeing a speeding up of the enforcement process?

Cat Little: I have to admit that I have not got any specific details on the pace at which it is changing our response to our work. Again, I would be very happy to provide further written detail after the hearing.

Q211 **Mr Baron:** That would be helpful if you could, because obviously you will appreciate the importance of the Committee understanding these issues, and progress in these specific areas is integral to the efficacy of our sanction regime.

May I move on to the Russian oil price cap, which was implemented only a week or so ago? How is it going? It is very early days, I know. Do you have sufficient resources? One is hearing whispers that it is a bit of a pain to implement. What is your assessment?

Cat Little: As you say, it is very early days. I should pay credit to the teams who have been working collaboratively with our global partners on this. It has been an incredibly complex piece of work and it was in the making for several months. It is a great achievement that they have been able to get to this position. It has two main purposes, as you will be aware. The first is to make sure that we are able to minimise revenue for Russia from oil, and the second is to make sure that we can increase and manage the flow to third countries, whereas previously we have had real challenges in making sure that flow was continued.

It is fair to say that it is very complex, and that is why we have established a dedicated specialist team. There have been some challenges, I believe, particularly in relation to maritime shipping and insurance industries. We are working very closely with our colleagues in the US and the EU to make sure that we understand the concerns of the specific Governments involved. Obviously, we are one week in, but so far we expect it to have the impact that we would hope. Certainly, when we look at the average price of Brent crude oil at the moment, we see that it is about $80. There are some early indications that the price cap is having an impact on average trading and prices for Russian oil.

Q212 **Mr Baron:** Is that what you would consider to be the most immediate effect of the announcement of the price cap? Is it higher prices? What are the immediate effects as far as you are concerned?

Cat Little: Other than, as I say, some very early indications about the impact of the price of Brent crude oil on Russia, we have not seen a huge amount. It is incredibly complicated and I think we need to give it more time to evaluate the impact overall.

Q213 **Mr Baron:** Fine. You talk about it being a very complex arrangement for enforcement, understandably, but what implementation challenges do these kinds of measures pose, and are you confident that they can be overcome?

Cat Little: On the sorts of challenges involved, the first is around working with maritime and shipping partners to ensure that we can actually continue to see the flow of supply globally. That is not a straightforward thing; it involves lots of different types of maritime and insurance legislation, in lots of different territories around the world. As we have seen in the past week, that has been tested, particularly in the Bosphorus strait, so those are real-life challenges, which our colleagues around the world, and in the supply chain, are grappling with.

Secondly, on minimising the revenue for Russia, which is an important part of this, we have set the price at $60. That was done very thoughtfully and carefully, with our partners, but we must keep that under constant monitoring, because, obviously, the volatility of oil prices overall means that we might have got that figure wrong. The last thing that we want to do is fail in our desire to minimise revenues for Russia.

Q214 **Mr Baron:** One component of the oil price cap is a ban on the provision of services—insurance brokering, shipping and so forth. What assessment have you made of any longer-term impact or harm to the international competitiveness of London's insurance market? Has any work been done on that, and are you seeing any of the early signs of anything?

Cat Little: We have not seen any immediate impact, but, certainly, we are thinking about doing some further work on this. It is clearly a question that arose quickly following the implementation last week, so we will be considering further work over the coming weeks.

Mr Baron: Would you please keep the Committee informed of that as you progress?

Cat Little: Of course.

Q215 **Mr Baron:** Great. Staying with the issue of forecasting and trying to assess any longer-term implications, but broadening that out, regarding the Treasury's effectiveness at forecasting, can I just ask you—or suggest to you—that forecasting has not been a strong point of many Government Departments? We only have to look at the Treasury's forecasts regarding inflation, compared to the OBR's, to see a very big difference.

Now, I am not saying that one is right or the other is wrong, but is that an area that concerns you, given that, while one always takes forecasting with a pinch of salt, it is important when it comes to the allocation of resources? You are not very good at it. Why do you think that is?

Cat Little: If I may start with that—others might want to add to it—we are very concerned about the accuracy of financial forecasting. The Government finance function, which I am the head of within the Treasury, has recently undertaken an in-depth review of why forecasting has been so difficult, particularly over the past couple of years.

We have disaggregated our financial forecasting across cash, capital and resource, because the type of forecasting undertaken is very different for each of those types of expenditure, and the same is true, of course, of demand-led forecasting for AME. For those three particular types of forecasting, the Government finance function has now produced best-practice guidance notes on what we expect Departments to do. For many years, we have insisted on Departments returning their outturns within 1% of their six-month forecast, and for cash forecasting, we run a penalty regime to try to incentivise Departments to sit within 1% of overall cash forecasting.

Certainly, in the past couple of years, it has been incredibly difficult to forecast much more volatile areas of spend, and we have particularly seen that in the Department of Health, which had very big challenges in forecasting demand for testing and vaccines in particular. However, that is something that we care very deeply about, and we have dedicated a lot of our time, through the finance function, to providing guidance and best practice on it.

Q216 **Mr Baron:** We are all aware of Galbraith's comment that "the only function of economic forecasting is to make astrology look respectable", but you have a choice, do you not? Do you drill down and commit more resources to make for more accurate forecasting—I am talking across the financial piste, with regards to your forecasts—or do you accept that trying to predict human behaviour when it comes to spending etc. is a nigh on impossible task, particularly in these volatile times? It sounds as though you are going for the former.

Cat Little: We are investing some resources, but quite a lot of it is investing in skills, modelling and techniques to allow us to refine what we do. I should say that not all Government forecasting is bad. We have monthly forecasting league tables, which we review within the Treasury, and we have a number of Departments who are very good at forecasting. Of course, if you have got historic trend analysis and information, which allows you to build more predictive forecasts with narrower ranges in the forecast fans that we produce, then you are more likely to have more accurate forecasts in the future. It is important that we have ranges. The big question is what you do with that information, and how you manage the financial risk associated with the ranges within a forecast bound. That is where every single month we work with Departments and Ministers to make decisions about what we think the impact will be in any given financial period for the reserve and for financial pressures, and therefore what we might do about it.

Q217 **Mr Baron:** Final question: why do you think it is that the Treasury's inflation forecast is so wide of the mark compared to the OBR?

Cat Little: Cat might know something different from me, but I am not sure that we do an inflation forecast that is different from the OBR's. Cat has given some excellent answers about forecasting within spending, but the main answer on forecasting is that we do not do macroeconomic forecasting, per se, in the Treasury. It is done by the OBR, as per the decisions in the 2010 changes. The OBR forecasts inflation and we use it, but unless I am missing something, I think that is it.

Q218 **Mr Baron:** So are you saying you make no official forecast for inflation at all?

James Bowler: No.

Q219 **Danny Kruger:** I think I am last, so the end is nigh, and you can relax—that is how I catch you out. I want to follow on from John's question about forecasts and energy prices, and then I have a question or two about public spending. Mr Bowler, the whole premise of the Chancellor's autumn statement was that inflation is going to fall. The public finances, I think we are agreed, depend on the assumption of falling inflation and, in particular, falling energy costs—very rapid falls in energy costs next year.

I am still trying to understand why we are so confident that that is going to happen. In recent weeks, we have had the OBR and the Chancellor in, and I asked them both the same question. The Chancellor said he trusted the OBR, and the OBR said it trusted the market, which is predicting this fall—although I noticed this weekend that electricity costs have spiked rapidly. My first question to you is, are you factoring in recent rises in energy costs? Do you think that the forecasts need to change in light of what is happening in the energy market? Secondly, what is your answer to the question of why we should assume there is going to be a dramatic fall in energy costs next year?

James Bowler: I'll ask Mr Duffy to come in as our expert on energy. I would say that the very recent spikes are about weather. We have had a surprise on the downside with a milder November and then on the upside with December—but I might be wrong. In terms of a forecast going forward, there is the initial shock and then this country and others adapting, learning and gearing up for that shock. That is part of why the volatility should come down. Phil, do you want to pick up from there?

Phil Duffy: I would start by saying that about half of the inflationary pressure is from energy; the rest is from wider inflationary pressures. We do not forecast, but no one is proposing a huge fall in prices next year. Arithmetically, if prices stay high, they begin to drop out of the inflation numbers. That may be one reason why we can still have very high prices but quite low inflation in future years.

On the actual prices, I would make two comments. First, no one, including the regulator, forecasts more than three years out for energy, and any attempt to do so has proved futile in recent years. Secondly, the prices are incredibly volatile right now—I mean, 25% day-on-day moves are not unusual. Just in the past week, we have seen the price yo-yoing back and forth.

A lot of that appears to be because the market is not very heavily traded on an intraday basis. As I was saying to Dame Andrea Leadsom a moment ago, we have this obligation to forward purchase, so the volumes being traded on a day-to-day basis are now much lower than they would be historically, because of the regulatory changes.

If we look at the forward curve for the year ahead—which is sort of real, because people have to buy gas and electricity for the year ahead—the price looks quite high and quite flat at that high level, which implies a dual-fuel typical price cap somewhere in the order of £4,000, so not particularly lower than we are experiencing currently. There is no illusion, certainly in the Treasury or in BEIS, that we are about to see some enormous fall in price. A lot would have to go right for that to be true—a Ukraine settlement and an expansion in supply from North America, and those feel like very optimistic, unrealistic scenarios.

Q220 **Danny Kruger:** Thank you for saying that, and I rather agree. Remembering the report the OBR put out with the autumn statement, it was predicting negative inflation in energy costs next year, so it is obviously predicting significant falls in cost.

Phil Duffy: The key thing that I would observe between the OBR's forecast and now is a steady but consistent rise in the forecasts for the next 12 months. If we look back to the time of the autumn statement, we were predicting a lot lower prices, but we have seen them rising and rising over that period—today, per therm, gas is about 346p, which is quite a high level compared with historical averages. That leads us to think that the next year will be quite flat.

Q221 **Danny Kruger:** Okay. Imagining if not the worst case scenario, a bad case scenario, in which energy prices do not come down as much as we want them to, and given the tight headroom that the Chancellor has allowed himself and the new fiscal rules on borrowing, do you accept that we will not be able to borrow our way out of a sustained energy price rise—at least, not falling energy prices—and that therefore the books will have to be balanced through tax rises or spending cuts? I appreciate you cannot forecast where the balance will be with those, but is there any indication in the statements that the Chancellor has made or the guidance you have had of how reconciliation might be made if the numbers do not add up?

Phil Duffy: Others can deal with the reconciliation. On energy, the Chancellor has signalled very clearly in the autumn statement and subsequently that our intention is to move away from having an uncapped Treasury liability for the future direction of prices and, therefore, to move to systems that provide greater certainty of our fiscal exposure on energy. That could mean, for example, moving away from a price cap to a fixed discount on the price.

We are in the advanced stages of concluding our review of the business energy scheme. You will recall that there is no scheme from the next financial year onwards, and we have agreed that we will publish the outcome of our review before Christmas. We are looking at that carefully.

We have also set out a route forward for next year for consumers, which will see a higher price cap. The Chancellor's logic is that, faced with the grave situation on the European continent, it is right to incentivise the people who can to become more energy-efficient. You will have spotted that in the autumn statement, he added up to £6 billion extra in the next SR period for energy efficiency. He is looking hard at the taskforce idea to think about how we can do that as a whole. That points to a progressive reduction in the public subsidy and to an expectation that more businesses can start to take their own measures to reduce energy consumption across their business in the coming years.

Q222 **Danny Kruger:** Thank you. Moving on to spending and the performance of Departments in particular—I am not sure who this is for—I am interested in your collective sense of the appropriate balance of power between the Treasury and the spending Departments. Where do you think that lies at the moment? Do you think that you have more or less freedom as a spending Department vis-à-vis the Treasury than you did a few years ago? As a Treasury, do you think that you are pretty laissez-faire with Departments? I noticed that you talked about penalty regimes, if Departments do not spend right. You have outcome delivery plans in place—presumably, targets for delivery. How tight is the leash that you are keeping Departments on at the moment?

James Bowler: Cat can answer this, but a half-sentence answer is: friendly but firm. If you lined up my perm sec colleagues here, I do not think that they would use the word laissez-faire.

Cat Little: I entirely agree with that, James. We have in place what we called an earned autonomy regime with Departments. It is something that we have really refined over the last couple of years. Every year, we undertake an assessment of the quality of financial management within Departments, and those Departments that we assess as having higher levels of financial quality and expertise have higher delegated authorities from the Treasury. Every year, we review those at the bottom of the league table and those at the top, and we make a commensurate and proportionate judgment on how much autonomy to provide them. I think the thing that most Departments would say is that our controls—the way in which we delegate authority to Departments to spend—are within a framework that is very clear, and within an earned autonomy regime that is transparent, fair and mutually agreed each year.

Q223 **Danny Kruger:** Which are the Departments that you regard as deserving of more autonomy than others at the moment?

Cat Little: There are a number of Departments that have been in our higher financial management ratings over a couple of years. I would mention two in particular. One is the Department for International Trade. Secondly, this year the Treasury has also been in our top quartile.

Danny Kruger: Well done, the Treasury!

Cat Little: It is something that we are very proud of, and I give credit to our finance—

Q224 **Danny Kruger:** What proportion of Government expenditure is the Department for International Trade, I wonder.

Cat Little: Obviously, the Department for International Trade has a relatively small budget, but I think that some of the practices that we have seen, and best practice around business cases in particular—

Q225 **Danny Kruger:** They are very good at spending not very much money. Okay—that is helpful. My reason for asking is that I am interested in the timeframe in which the Government allocate budgets to Departments, because I am conscious that when we do something involving large-scale capital expenditure on infrastructure—when we build a new trainline or airport, if we ever build another airport—we are prepared to spend over decades and make forward commitments well beyond any spending cycle, budget cycle, or indeed Government. What is the longest that we could do that in revenue spending, particularly on social programmes, and why do we have such small budget cycles for social spending? My question is whether we can do better.

Cat Little: The simple answer is yes. I would particularly point to a couple of things. First, for infrastructure and capital spending, I think our view would be that it is much better to be able to set out long-term plans, especially where you have very long-term programmes or you have repeatable infrastructure, such as schools. Schools are a good example. We have a 10-year plan regularly set out for commitments to schools, but we obviously have to balance that with the fiscal costs, and not tying the investment strategy and the choices for capital spending for too long. That is why we try to get a balance between setting out specific medium and long-term plans, where you have long-term infrastructure and market supply arrangements, versus shorter periods where we think that there is a choice that the Government might need to take in order to balance the public finances. We have also highlighted the need to speed up the way in which we make investment decisions in Government. We recently produced new guidance for Departments on how you streamline decision making to support faster approvals for programme expenditure.

Q226 **Danny Kruger:** Thank you very much. My last question may be for Ms Caffyn. I am interested particularly in revenue spending, not investment and capital. What I have been trying to get at is that I am a huge admirer of the model of payment by results, or outcomes-based commissioning, which some Departments still use. We have seen it growing over the last 10 years, but it remains pretty small in terms of the quantum of expenditure. As I understand it, what we are talking about here is when the Treasury or a Government Department commits to paying out on evidence of results that may be some years hence, particularly in complicated social programmes beyond this budget cycle, but the difficulty is that the Treasury is reluctant to make a promise to pay on evidence years hence. This model potentially enables a programme, particularly one in civil society—not even in the public sector—to raise money privately to deliver work, but it can raise that money only if there is an expectation that there will be a payment on results some years down the line. Is that something that we can do more of, or is there some Treasury financing rule that prevents it?

Cat Little: There is no financing rule that prevents it, and there are several examples of where we use both payment by results and social impact bonds to do exactly what you have just described. What we would say is that there have been mixed results. We are expecting one of the latest funds that DCMS oversees to do a fuller evaluation of how social impact bonds and PBR are applied in social programmes.

My personal view is that PBR is best applied when you have a very good quantifiable baseline of the service provision and the outcome that you are trying to achieve, because when you do not have that it is incredibly hard to measure the quantitative difference that the investment or the changing activity has generated. We have seen some really serious issues with PBR applied to two revenue projects. A good example would be the probation service most recently, where the complexity of the payment mechanism—the inability to measure the difference to the baseline—meant that it was incredibly difficult for us to ascertain when and how to make payments. It led to the non-viability of the market. I have to say that I am personally sceptical.

Danny Kruger: Okay, but there are other examples of enormous success in demand reduction, and genuine costs savings, particularly in health. The social prescribing model has been very successful in doing that. I think that you are holding these projects to a higher standard than you hold some public expenditure, because of course you have to imagine what would happen otherwise. It is not as if the current model of chucking money at projects before the results have been delivered necessarily delivers the success that we want either. I think that there is value in this approach, although I take your point that it is not always successful.

Chair: Thank you, Danny, and thank you, Cat. We enjoyed the fact that the Treasury is leading by example, and you are the top-ranked Department, or the second top-ranked Department, in terms of your ranking of how efficiently Departments manage their finances. We also enjoyed the fact that the Department for International Trade was on that list, which is where James was previously permanent secretary. You have piqued the Committee's curiosity and we would like to request the full ranking, please, so that we can see which Departments are at the other end of the list.

It has been a very interesting session, after a very busy year for Treasury officials, I imagine. In our annual touching base with you to ask you questions about the year, we salute the hard work that must have gone into dealing with four different Chancellors and so many different fiscal events, not to mention Putin's evil invasion of Ukraine. It has been a very interesting and informative session. We have asked you for a number of follow-ups. Thank you very much for sparing the time to answer the Committee's questions this afternoon.