House of Commons

# Treasury Committee

## Oral evidence: Budget 2025, HC 1349

Wednesday 5 November 2025

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Watch the meeting

Members present: Dame Meg Hillier (Chair); Chris Coghlan; Bobby Dean; Jim Dickson; John Glen; John Grady; Dame Siobhain McDonagh; Catherine West; and Yuan Yang.

Questions 227 to 311

### Witnesses

I: Rt Hon. George Osborne CH, former Chancellor of the Exchequer, and Rt Hon. Sir Vince Cable, former Secretary of State for Business and Trade.

# Examination of witnesses

Witnesses: George Osborne and Sir Vince Cable.

Q227 **Chair:** Welcome to the Treasury Select Committee on Wednesday 5 November 2025. This is part of our sessions on the Budget, which is coming, of course, on 26 November. As part of that, we have two former economic Ministers at Cabinet level in front of us. We are pleased to welcome the right hon. Sir Vince Cable, who served as Business Secretary in the coalition years, and the right hon. George Osborne, who served as Chancellor during that period—I think six years in total. Welcome to you.

I want to make it clear that today we are talking about the 2025 Budget, so we are not particularly going over your record in government—tempting though that may be—but we are keen to hear what it is like for people who were in the hot seat at the time.

Perhaps if I could start with you, Mr Osborne, you have been in the hot seat. You had to face all the slings and arrows, what the media say, all the speculation and the lobbying from colleagues, and you are one of the handful of people alive who have actually been through that, so that is one of the reasons we wanted you here. Can you give us some insights into the factors the Chancellor will be having to consider right now, and what it feels like in the Treasury?

***George Osborne:*** First of all, thank you very much for having me back. I have lots of happy memories of young Labour MPs like Wes Streeting and Rachel Reeves quizzing me at the Treasury Select Committee.

The thing about a Budget is that gone are the days when we lived in a closed economy where everyone tunes in on Budget day, as I remember from my childhood, and that has a direct impact on the currency and the stock market and so on. It can have an impact on those things, but that is normally when the Budget has gone wrong. Today, and certainly when I was Chancellor, it is an all-of-Government organising event. In my day we had a spring Budget and an autumn statement. Gordon Brown and Alistair Darling before me had a pre-Budget report. In effect, you have two Budget-like events a year, and they are very useful organising moments for Government to arrange their domestic policy around.

The Chancellor is obviously at the centre of things, negotiating with Cabinet colleagues about what is going to be in the Budget, and is then very specifically working in partnership—hopefully—with the Prime Minister. There is nothing that can appear in the Budget that the Prime Minister does not want to appear. And there is nothing that can appear in the Budget that the Chancellor does not want to appear. So you have a double lock on these key events.

Ultimately, the decision making is in a very tight circle. In my case—you will turn to Dr Cable—there was this other key element, which was that I could not announce anything the Liberal Democrats would not support in the Division Lobby later. There was a negotiation inside the coalition, but that was specific to then. In a single-party Government—I did two Budgets in a single-party Government—it is really a negotiation inside Downing Street.

We can come on to all the different considerations, but there are around 4,000 decisions in a Budget. Many are on a tractor beam of things that, frankly, almost anyone doing the job would probably do. So you are looking at, which things are distinctive for my party and my Government? Which are distinctive for me personally as Chancellor—my personal priorities? What you ideally want, which is probably not the case today, is for your first Budget to set out the stall, and for your second and third Budgets to top up, reinforce and build on what you have announced. You do not really want your second Budget to be as unknown as your first Budget.

It is also about trying to maintain consistency while you have all these things swirling around you: the OBR forecast, the mood of the parliamentary party, the politics inside the Cabinet. The main thing, which often gets lost, is in some ways the opening sentence of the Budget. People often focus on the last sentence or the big reveal, which most Chancellors have at the end. What is lost is the first sentence of the Budget: what is this Budget about? Can you sum it up in a sentence, so that you can explain to Parliament, the media and therefore the public what this whole mass of measures is really about?

Q228 **Chair:** Sir Vince, you had to go out and explain a Budget that was set by a Chancellor not of your own party, although you obviously had to buy into that. What was it like from your perspective?

***Sir Vince Cable:*** First of all, I add my thanks for the invitation. I used to be a member of this Committee, in the days when Gordon Brown was the Chancellor.

**Chair:** Everyone is reliving their old glories, which were clearly in this Committee. That is good to hear.

***Sir Vince Cable:*** George has given a very fair assessment of the process. There have been a lot of criticisms of the coalition on policy grounds, but I would defend it: the process was actually very good. As a result of being able to resolve issues internally, we were able to provide five years of stable Government around a framework that George has just described.

I will just make one comment, which I think links to the present day. I was told in the first few days of the formation of the coalition Government, by all the senior economic advisers to the Government—senior civil servants— that the overriding concern for the country was the pressure from external bond markets and that, whatever else we did, we had to observe strict financial and fiscal discipline. That provided a motivation for the initial Budgets, and beyond, and a recognition that we were operating in a goldfish bowl: we were under constant supervision from external markets. I am very conscious that the present Chancellor is under exactly the same pressure.

Q229 **Chair:** I think 2022 really underlined that as well. We have the Budget coming up, and the Chancellor has been very clear: she repeatedly talks about growth and the focus on growth. Is that the right strategy to get the country's financial situation on track, Sir Vince?

***Sir Vince Cable:*** I wrote an article a few months ago—I struggled to write it—called "What Rachel is Doing Right". I think there are several things that are relatively positive. The first is the acceptance of the fact that you need to operate within a disciplined financial framework, with an independent central Bank. Secondly, she managed to do what we didn't do in coalition, which was to prioritise public investment and to give it a role within the fiscal rules, counting public assets in the counting of net debt.

The other thing was to give a sense of direction that the overall bias of public spending and taxation is essentially to defend the interests of old fogeys like me, and that the new Government had to redirect the priorities elsewhere. You can argue that they have dealt with this rather cackhandedly with the winter fuel allowance, which probably should have been treated as a taxable benefit rather than abolished; none the less, the direction was right.

I would add one other thing. Although I think there is a general consensus that the economic position at the moment is pretty dire, it is also dire in all other western democracies, for rather similar reasons. Productivity growth is very slow everywhere—possibly with the exception of Spain. Almost all western countries have public debt that is unsustainable—particularly extreme in the United States, but a widely shared problem.

We have this exceptional problem of vulnerability to attack by external creditors because we are very much reliant on external borrowing as a country. But trying to make a fair assessment—I came here not to try to score partisan points—I think we have to acknowledge that the Chancellor has made some correct moves and is genuinely constrained by factors that apply to all western democracies at the moment.

***George Osborne:*** I agree with a lot of what Vince is saying and I have quite a lot of sympathy for the Chancellor's position, but I think in that situation it is all the more important to have a clear plan. When I was doing the job, the US Treasury Secretary at the time, Tim Geithner, had a great phrase—"Plan beats no plan." People can argue about what happened back then, but if the Government can communicate a clear sense that it has got a plan—you might not like the plan, but it has got a plan—that in itself instils confidence.

I would say one of the challenges at the moment is that it is not really clear what the priorities are. You say growth is the priority. The Chancellor gave a speech yesterday in which growth was not the priority—cutting NHS waiting lists and reducing the deficit and the cost of living were the three priorities. And that is different from what the Government said a year ago. So I would urge them to settle on a set of priorities.

The thing about growth is, there is not some big lever on the desk of the Chancellor or the Business Secretary that you can just pull and you get growth. And there are lots of external constraints to it. Nobel prize-winning economists will vehemently disagree with each other about what produces growth and what are the right ingredients—whether you should deregulate or regulate, spend more public money, cut taxes or whatever it happens to be.

I would not take issue with Vince, but there is a bit of an outlier in the west at the moment—maybe not so much this year because of its self-inflicted wounds with tariffs, but the United States economy has been more productive over the last four or five years than the western European, including UK, economies. And something has happened. There is a sort of detachment.

If you look back to the 1990s, or the 2000s, or the period when we were in office, obviously the United States was in some degrees more dynamic, a bit more capitalist—the tech sector was emerging—but you always felt we were within touching distance, and certainly the capital city here, London, was a contender for the global financial centre. There is definitely a feeling that I detect—and I teach at Stanford University in California—that the US has pulled away. The productivity numbers in the US are markedly better than Europe.

Therefore, you have to ask yourself, what is it that they are getting right? Their political system is quite dysfunctional and unable to kind of organise things particularly well. The big innovation that is happening in artificial intelligence. I would observe it is interesting that so much of that is coming out of the United States. It is also coming out of China, but it is coming out of the United States, and it is not even necessarily coming from the incumbents. It is coming from brand-new companies that two or three years ago barely existed, and suddenly are worth more than much of the FTSE put together. So I think it is worth looking at what the US is doing to—

Q230 **Chair:** Do you think the Government are right to lean into AI?

***George Osborne:*** I think the Government are right to lean into AI, not least because it is happening anyway, so you want to harness it to the best of your advantage as an economy.

Q231 **Chair:** Will it create growth or just mean that people lose their jobs?

***George Osborne:*** I think it is possible that it might do both. I think it will lead to productivity gains. It might help enormously with this challenge that Vince alluded to: how do you make these overly indebted western economies deliver better public services? But it is obviously—well, I say "obviously"; it seems to me obvious that it is going to lead to a massive dislocation in jobs. Historically, if you look at the UK, and if you look at the 1980s, or the post-war period, or the Victorian period, when there is a big change in technology, there are a lot of casualties. Frankly, although Government talks about retraining people, in practice it has quite often parked people on to incapacity benefits.

Q232 **John Glen:** It is nearly 10 years since the coalition ended. If you look at the level of GDP growth, I think there has been only one year when it was above 2.5%, apart from the aberration of covid and immediately after. Is there not a risk that the Chancellor, Rachel Reeves, faces a situation where society's expectations are bound by a level of welfare and investment in public services that is in direct contradiction with, and not compatible with, the level of performance in the UK economy, and that essentially there is a disconnect between the politics and the economic reality? Do you recognise that, and if you do, how does she reset?

***George Osborne:*** That is addressed to me?

**John Glen:** Yes.

***George Osborne:*** I think up to a point. Again, not unlike Vince, I am quite un-partisan these days, or at least I attempt to be. The increase in public expenditure and taxation that the UK has seen started in 2019; it did not start with the election of a Labour Government last year. That is when GDP starts to grow, that is when state spending as a share of GDP starts to increase, and that is when taxes start to increase.

You could say that we are moving to a more continental model of higher tax and higher public expenditure, but with a whole load of pressures, much driven by demographics, that mean that, fundamentally, that is the new resting place we are going to find ourselves in. But the trade-off to that is probably a less dynamic economy over time. That is going to be the challenge you allude to.

One of the big tasks for any Government and Parliament is to constantly look at how you can try and reform your public services. When I was an Opposition MP under Tony Blair's Government, a big theme in that Government was domestic reform of education, healthcare and welfare, and so on—I would argue that the coalition did quite a lot of that as well, some successfully, some less successfully.

But I feel that quite a lot of the public service reform programme, which helps to address this problem of affordability, has run into the sand a bit. Again, it is not really a party point; who's got the big new ideas on reforming education, which used to be the big battleground when I was in Parliament? Who's got the big ideas on reforming healthcare or welfare? There have been the parliamentary problems for the Government this year. That seems to me a missing part of the British political conversation at the moment.

Q233 **Chair:** We are going to move on to some specifics, and one specific thing for you, Mr Osborne. You set up the Office for Budget Responsibility, and there has been a lot of swirling noise around that, and rumours that the Chancellor would rather have one forecast a year. What are your views on that?

***George Osborne:*** Look, when I set up the Office for Budget Responsibility, it was an Opposition idea. It is quite hard to remember that back before it was created, the Chancellor of the Exchequer would announce the growth forecast, the inflation forecast and the forecast of what taxes would raise and what planning reforms would deliver in terms of GDP growth. They would be Treasury numbers, and the Treasury would not show any of its workings.

In fact, once in opposition that all leaked, and people started to say, "Hold on—how did they arrive at these sums?" So there was a big credibility problem around Government forecasts, and the OBR was an attempt to provide a neutral and independent forecast. That does not necessarily mean that it will be right, because forecasts are hard to get right, but it is independent.

Q234 **Chair:** Do you think it should have two forecasts? Would you have any sympathy for it to move to one?

***George Osborne:*** I think the problem is not how many forecasts. I think it should have two a year. I think it was the Labour Government in the 1970s who set the precedent—in fact, it was Tony Benn who insisted that the Government produced two forecasts a year.

I want to make two observations about the OBR. In part, the Government are a victim of having set a very narrow headroom, so every single change in any part of the OBR forecast puts them into trouble, potentially. Therefore, Treasury officials, quite understandably, go to the OBR and say, "The Indian trade deal that the Prime Minister signed should add 0.3% to GDP, not 0.2%," because it makes a big difference if you are putting a Budget together—it probably means you can avoid one of the difficult tax rises that you might be anticipating.

At the same time, I have enormous affection and support for the OBR. I think the OBR itself can back off a bit with having these conversations with the Government and trying to second-guess, "What does this planning reform do? What does this Indian trade deal do? Will these immigration changes affect it?" You get drawn into micro-forecasts, which, when they aggregate, create quite a problem.

I think if both sides would step back a bit and get back to the idea that this is an independent referee—by the way, principally for parliamentarians, to say, "An independent forecaster has given us a view." The Government, by the way, are entitled to reject that view in the Act, but all Chancellors have accepted the OBR forecast. Then, it is a sort of level playing field so that then you can have the partisan argument.

***Sir Vince Cable:*** There is a danger of the OBR just becoming a kind of whipping boy for political failures. It is actually more necessary than ever, given the precariousness of our external position. I think what has happened—and I don't think it is the fault of the OBR—is that it has moved from a position of just marking the Government's exam papers to setting the exam questions, and they are very difficult questions. Things like projecting future productivity growth, which are virtually impossible, are probably things that should be done inside the Treasury, rather than subcontracting to the OBR.

**Chair:** Thank you. Could we get tighter questions and answers, because we are hoping that you might have some thoughts about what could be in the Budget on 26 November.

Q235 **Jim Dickson:** A very important one: obviously, the central focus of the Budget is how the Chancellor can increase tax revenues to pay for investment in public services and other priorities. Do you have any thoughts on what sensible measures to increase revenue might be—perhaps improving the tax system at the same time?

There is lots of talk around things like property taxes, how you treat pensions from a taxation point of view, food—Mr Osborne, you might not want to be reminded about how you changed taxation on food—but what ideas might it be sensible for the Chancellor to adopt?

***Sir Vince Cable:*** I think a substantial tax increase is unavoidable. There is a political problem of making this promise before the election, but I will put that to one side. In terms of economic necessity, it is very difficult to see how it can be avoided.

Before giving more specific suggestions, we need to try to get away from what is presented as a truism that somehow Britain is overtaxed. Our tax level in relation to GDP is fairly close to the OECD average. Part of the problem is that we have an aspiration for Scandinavian public services but we don’t have Scandinavian levels of tax to pay for them.

As to what has to happen, it is almost certain that the Chancellor will have to use a broad-based tax—income tax is the obvious one—but I would make the point that these things are not only easier to present politically, but better policy if combined with tax reform. We have an extraordinarily complicated and perverse system of taxation. If an income tax rise were coupled with integration of the employee national insurance system—partial integration, or a stepping-stone, effectively, to make the two the same—that would be a very positive step.

The other issue you mentioned was property taxation. I think you are absolutely right that the Government will move in that direction. I should have a patent out on the proposal for a mansion tax; something of that kind may well happen. It would be much better if it were done as part of making the property tax system more coherent generally, perhaps through a move to proportional taxation of property values, taking in—hopefully to get rid of—some of the worst features of the stamp duty system. That would be much more satisfactory than just doing ad hoc, small changes that annoy people and don’t necessarily create a better or fairer tax system.

Q236 **Chair:** Could that be done in time for the ’26 Budget? Could that be done in time to bring money in—if that wider approach of making such changes to property taxes in the round is taken? We are actually discussing property taxes next week.

***Sir Vince Cable:*** It would be difficult to do it in one swoop, but I certainly would support the move to having taxation on higher-value property. It is something we discussed in the coalition, and we came to a reasonably good compromise at the time, but we now need to refer to it.

***George Osborne:*** I think tax rises are inevitable. I would say you have to put them alongside expenditure reductions and constraints. The Chancellor is getting it right in saying, "I've set out fiscal rules, and I am going to stick to the fiscal rules." I think this Government and the country become completely unanchored, and vulnerable to the bond market pressures that Vince was talking about, if they just abandon those rules. Having set the rules—they are pretty sensible rules—you then face a problem. You have a Budget deficit of almost 5% and debt at 100% of GDP, so to say it is all going to be done with tax is as wrong as saying it is all going to be done with public expenditure cuts.

I was the Chancellor who increased VAT from 17.5% to 20%, and introduced additional taxation of pensions, higher stamp duty on higher-value properties and so on, so I also did tax increases, as well as the things I am more known for, which were the expenditure reductions. It should be a mix and it would be a very one-sided and mistaken Budget if it were all on tax rises.

Then you face the question of, "Well, what do we do?" It is obviously easier to go for one of the big three taxes of income tax, national insurance or VAT. Of course, the Government are constrained by their promise; maybe they will choose to break that promise. It is difficult to break a manifesto promise—speaking from a political point of view—but the Sunak-Boris Johnson Government increased national insurance having promised in their 2019 manifesto that they would not. They used covid as the reason why.

That passed through Parliament—it was subsequently reversed by the Truss Government, and then retained as one of the few things of the Truss Budget that was retained. You can get away with that—well, I am not sure you can get away with it, but that Government passed it through Parliament and if they had made it to the general election they might have been able to argue why it had been necessary. You can use extenuating circumstances.

The trouble is, if you don't use one of the big taxes, you are left with lots of little ones, and I would argue that part of the problem last year was that. An increased capital gains tax or changes to the non-dom regime might be individually defendable, but put them all together and they give an overall impression of the UK being quite anti-enterprise or anti-foreign wealth. The risk is that if the hole is substantial in this Budget and the Chancellor has to do 10 taxes, that is pretty messy and falls foul of what I was saying earlier: what is your one message that you are trying to communicate?

Q237 **Jim Dickson:** Sir Vince, you wrote that a 1% rise in VAT would raise £7 billion and you felt that was still below what other countries were capable of raising through that measure. Do you think that the UK ought to perhaps take that option?

***Sir Vince Cable:*** Value added tax is 25%, I think, in every one of the five or six Scandinavian countries. If we want those levels of services, that is the kind of tax structure one would have to think about. I would not recommend it for this Budget, for the obvious reason that it would make a significant impact on the cost of living, inflation, in the short run, and would be very difficult to reconcile with the other objectives of Government.

Q238 **Yuan Yang:** You both mentioned the mansion tax and revaluing some council tax bands, which was a coalition Government proposal from back in 2012. I am curious about the political economy of that. What were the difficulties in discussing that within the coalition and getting that enacted? What do you think would be the challenges now?

***George Osborne:*** The main challenge was that the First Lord of the Treasury overruled me at the time, so it didn't happen. We managed to keep it secret at the time, but what we had agreed—I say it now, with the passage of time—inside the coalition and between myself and my Liberal Democrat colleagues Vince and Nick Clegg and Danny Alexander, was that we would introduce two additional bands of council tax for high-value properties—I think, from memory, one for houses worth more than £2 million back then and one for houses worth more than £5 million, of which at the time there were 55,000 in the country out of around 24 million homes. Almost all of which were in West London, it has to be said—now represented by Labour MPs, I should point out.

But the crucial thing was that the money raised from that was going to be used to reduce the top rate of income tax from 50p, which it had been in the last act of the Brown Government, to 40%—which is where it had been throughout the Blair Government. So it was going to be a 50% to 40% reduction in income tax and an increase in property tax to pay for it. And then, for perfectly good, sound political reasons—David Cameron felt the Conservatives had promised not to have a mansion tax, under pressure in opposition from Dr Cable and others, and he also thought in 2012 reducing the top rate of income tax from 50% to 40% in one go was too much politically, essentially—we settled on 45% and a series of small taxes, including taxes on hot food, to pay for it.

Q239 **Chair:** So it is David Cameron's fault that we had the pasty tax.

***George Osborne:*** Not David Cameron's fault. But that is a good example of tax reform being quite hard when you are trying to raise taxes. Tax reform is a great thing; everyone is in favour of tax reform, but you usually create losers. So it is generally easier to do tax reform when you are cutting tax and you can buy off the losers. Whereas if you are raising tax, extending VAT boundaries, that is much harder.

The simplest way to do a property tax in the UK would be to do what New York State has or California has, which is just a percentage of the value of the house, which you pay each year. But that would be quite a revolution for the UK. And remember, you have to go and value all these properties all the time, which is a big, big challenge. I think when they tried to revalue council tax bands in Wales a few years ago, it was not very popular. So the idea was that you would have these two additional bands, but crucially, the money was going to be used to reduce taxes on high incomes.

Q240 **Yuan Yang:** Mr. Osborne, you mentioned at the start of that answer that the Treasury overruled you. Could you go a bit more into the detail of that?

***George Osborne:*** No, it was the Prime Minister who overruled me. I say "overruled me" but, you know, we are still very good friends and it was never that kind of relationship. He made sound political arguments about why it would be a difficult sell. It is a general point that I should have made at the beginning: Budgets when the economy is doing badly are really tough. The 2012 Budget was the toughest for me personally, and that was also the year when it looked like we were in a recession—I was off my fiscal targets. So the context in which you are standing up makes a big difference for a Chancellor.

Q241 **Yuan Yang:** Sir Vince, is there anything you want to add to that description?

***Sir Vince Cable:*** Your original question was about the political economy of this measure. The honest point that one has to acknowledge is that, although I advocated it, it does not actually raise very much revenue. That is why I would now argue that you probably have to go rather further. That is why—on the point George just mentioned—we should aim to move to a more proportional system of taxing property although, as he said, that is not at all straightforward.

The other politics point that we all had to deal with, including me—because even the Lib Dems had people living in very high-value properties—was people who are income-poor but asset-rich. There are ways of dealing with that. You can obviously downsize, you can use equity release, you can rent out a very large property. There are answers to it, but if that change were done—and I believe it should be done—there would be quite a strong political reaction from people in that position and you have to have an answer for that.

Q242 **Yuan Yang:** Mr Osborne, you mentioned that it is more difficult to raise than to lower taxes, and earlier that the Government are, to some extent, a victim of the low headroom—£10 billion in headroom, which is the same level as under Jeremy Hunt, post-2022, and a lower headroom than before the pandemic. Do you feel that it was irresponsible for Jeremy Hunt to cut national insurance by 2p? It would have doubled the headroom if he had not taken that measure.

***George Osborne:*** On the headroom point, he was a Chancellor at the end of a Parliament facing an election a year away, and he just had to get through one year and deliver. The political theory is that you want to land on the election day with no headroom, because you use your last Budget to deliver the headroom for either expenditure increases or tax cuts, depending on your party or your manifesto.

It is very different from the first Budget of a Parliament, where you hope to be the Chancellor for the whole of that Parliament, in which you deliver a big headroom so that you can deal with changes in the forecast and so that, in crude political terms, you have your war chest that your party will expect you to deploy as you get close to the general election. That may not be how it is supposed to be in the economic textbooks, but that is how it is in the political textbooks.

Last year, the Labour Government's error was that, having got elected with a big majority for a four or five-year term, you want to build a big headroom, you can weather the storms, get towards the end and do what you want to do to try to get yourselves re-elected.

I had a lot of sympathy for Jeremy Hunt. The political pressure on him from his own party was that he had to deliver something to try to help win the general election. I did not choose to reduce national insurance. It is a bit of a simplistic way to think about politics: "I have delivered a tax cut, therefore people are going to re-elect me."

I think that people want an overall sense: "Have you got a grip on the economy? Do you look like you are in charge of events? Am I feeling better off, as a person?" There was a cruel test that they used to throw at MPs in interviews: "What's the rate of national insurance?" The overall objective should be for people to feel better off and for people to feel that their economic future is secure with this Government. That is the confidence that they need to exude, which they are not currently exuding.

Q243 **Yuan Yang:** You mentioned what is in the political textbooks: the political incentive to spend down the whole headroom, in effect handing over to a new Government without any rainy-day reserves in case of turbulence. Under that logic, every five years there would be a running down of headroom, then a huge Budget, then a running-down over five years—the opposite of what a country would want for stable growth. How do we get out of that political imperative, which is caused by the current fiscal framework?

***George Osborne:*** I think you can get out of it. First, elections cost in democracies. That is just a fact of life. As I used to say to the Treasury, "Unfortunately, we have a general election." That is the nature of our system. If it were up to the Treasury, it would have no Budgets and no elections.

Other people will judge the coalition Government's message—or, given the election result in 2015, the Conservative message—on what came to be known as austerity or fiscal prudence, but it commanded public support at the time. I know that that is not how people remember it now, but it did, and it got us re-elected.

I would say that Gordon Brown in his early phase—"prudence for a purpose", "I'm paying down the national debt", "I'm using the mobile phone spectrum sales to pay it down"—had a very compelling message for a Labour Government: that you could trust the Government with the public finances. They were not immediately spending everything that they raised. I was in opposition at the time, and I remember that it was extremely hard to find our way through it. To your point, Governments that exude prudence, caution and small-c fiscal conservatism do get re-elected, as historically they have in Britain.

In the Chancellor's speech yesterday, she said, "I have reduced the deficit, cut waiting lists and the cost of living." In some ways, reducing the deficit sits above the other things. She could have said, "By reducing the deficit, by being fiscally prudent and conservative, I will be able to afford to help you with your cost of living, afford reductions in waiting lists in the health service and so on." There is more of a hierarchy there than just having them as "Three random things I want to achieve."

**Chair:** To try to get into some specifics, I will bring in Bobby Dean.

Q244 **Bobby Dean:** I was explaining to colleagues before this session that I wrote my master's dissertation on British newspaper reporting of the mansion tax, but I will not persist, although there are 1,000 questions that I would love to ask.

One thing I came across when doing that research was the Mirrlees review, which I am sure you will be familiar with. The IFS produced a report on tax reform. I was struck by something you said earlier, Mr Osborne: that most Budgets have 4,000 decisions, most of which many people will agree with, and then a few politically defining things that you want to do. That seems to indicate that you do not really want to look at a Budget as a moment to take a holistic view of the tax system.

It has become quite fashionable now for people to say that our tax system is a mess and that what we need is proper tax reform. What did you think when that Mirrlees review was issued? Did you just chuck it straight on a shelf and say, "This is politically impossible," or did you try to think more deeply about what proper tax reform in Britain would look like?

***George Osborne:*** I did attempt a number of tax reforms and tax simplifications. We created an Office of Tax Simplification, which has now been abolished. One example was a big simplification of pensions taxation, which was seen as getting rid of the requirement to annuitise, but which was actually a reform of taxation, essentially giving people more freedom over what they did with their pension. That was a big tax simplification and was kept entirely secret until Budget day because of its market sensitivity. I think generally it is regarded as having gone well.

The stamp duty reform that I did got rid of the slab system and cut stamp duty for 98% of people. It did increase stamp duty on higher-rate properties, which is the only thing that people remember. Then all the thresholds were frozen for years afterwards, and as a result, it has crept up again. So there were individual pieces of tax reform.

Q245 **Bobby Dean:** Those are quite small-fry reforms, are they not? What about fundamental reform?

***George Osborne:*** To be realistic, when I was shadow Chancellor we did a big review into a flat tax. The truth is that you can say, "We are going to abolish income tax and national insurance and create a single tax," but income tax has been around since William Pitt the Younger. There are good reasons why every Chancellor who has been in office for a while and wants to do their big tax-reforming Budget looks at merging national insurance and income tax, but backs away from it because it is just very, very hard to do.

Q246 **Bobby Dean:** You did set up the Office of Tax Simplification, as you said, so I guess you recognised that there was a need for fundamental simplification, but we have the most complex tax system ever now. Did you miss an opportunity?

***George Osborne:*** That is partly because Parliaments and Governments want to achieve all sorts of things. They want to encourage people to save for their pensions, and there is big pressure now. In Scotland, we want the Scottish Parliament to be able to set different rates of tax. There is pressure to allow English mayors to have more tax powers. All those things lead to complications. When you want to encourage particular forms of investment or saving and you create things like the EIS, all those things equal tax complexity. People say, "The tax codes got longer and longer," but the individual bits in it are things that broadly people want, such as tax breaks for enterprise.

Q247 **Bobby Dean:** Are the people who are calling for tax simplification or major tax reform just politically naive? Are we doomed to have an ever more complicated tax system as we have to appease all these different sectors in the economy?

***George Osborne:*** I think you would have to have a period in which money was flowing into the Exchequer—that is not the case at the moment—and in which that was the political priority of the Government. It was done in the late '80s by Nigel Lawson. I think the Blair Government would probably have had an opportunity to do it in their second term, but they chose instead to use the money that was coming in—the unexpectedly higher-than-forecast revenue—to increase expenditure on public services.

Q248 **Chair:** What, specifically, would you both do now on tax reform if you were in the Chancellor's hot seat?

***George Osborne:*** If you could, merge income tax and national insurance. It is sort of odd that we have two taxes on income, but of course they are taxed on different forms of income and different ages. It is quite complicated; I did look at it pretty closely.

***Sir Vince Cable:*** It goes back to your basic point: politics and economics are difficult to reconcile. I started my professional life teaching the theories of Adam Smith to economics students in Glasgow, then going down to the Glasgow city chambers in the afternoon and doing the opposite. I am afraid that that is the world we live in.

My one thought, trying not to be very academic about it, is that it is very easy to come up with how you would reform the property taxation in a perfect world, or how you would reconcile income tax, but if the Chancellor could choose just one area, income tax and national insurance is probably the best. It is also has the effect of bringing in new taxpayers, landlords and earning pensioners like me into the tax net. That would be one thing to do.

It is not difficult to think of areas in which there is a grotesque mismatch between the economics and the politics. To give one further example, we have cut fuel duty by 40% in the last 15 years or so, for political reasons. That is bad for revenue and bad for the environment. Any academic economist would say that we should be moving across to road user pricing, which we will need anyway when we have electric vehicles. But the politics of that are just very, very difficult.

***George Osborne:*** The last Chancellor who tried to increase fuel duty was me, but I got defeated by the Labour Opposition and Tory Back Benchers.

Q249 **Bobby Dean:** Sir Vince, we talked earlier about the growth in the size of the state, and Mr Osborne remarked that it really started in 2019. A lot of the time, we talk about this as if it is a political choice, but there has been quite a lot of demographic change in our society, with more money spent on pensions, more money spent on healthcare for pensioners, and more sickness benefits for people at the late stage of their career. Sir Vince, you also talked about this being one of the defining inequalities in our society between the generations. Do we need to be thinking about tax reform in that context, in a society that is changing?

***Sir Vince Cable:*** Absolutely. I am with George in believing that we should start off by being neutral between tax increases and public expenditure cuts. We have been trying to be dispassionate about it, but it is actually very difficult now to cut public expenditure. It is not just the ageing of the population, which is a very powerful driver; you have defence spending on top of that.

In dealing with demographic change, a future Government—I am sure that this is not going to happen in three weeks' time—will have to look at things like the triple lock. It was a wonderful idea when we did it: it was very progressive, lifted a lot of pensioners out of poverty and was very commendable all round. But it is not sustainable, and it makes no sense in the long run. You will have to move to a double lock or something.

This Government or the next will have to grasp the nettle, which Andy Burnham and Theresa May both failed to grapple with—I think we tried to do so in the Government—of trying to get people to pay for care other than through the council tax system. These are the kinds of big, meaty reform issues from which Governments keep backing away because they are too difficult, but precisely because of demographic change, they will have to be faced.

***George Osborne:*** May I give a couple of outstanding examples of cross-party co-operation in reducing burdens on the state? There was the cross-party co-operation on raising the pension age: a report was commissioned by a Labour Government and implemented by the coalition Government.

The auto-enrolment in private pensions has increased savings in our society; again, that started under a Labour Government and was introduced under the coalition Government. Tuition fees were commissioned by the John Major Government and implemented by the Tony Blair Government, and then there was a further top-up. There are various things on which the parties managed to co-operate, in a way that we now take for granted.

Q250 **Chair:** With the state pension age, it was your Government who increased it at shorter notice, giving people less time to plan. That was a deliberate decision, presumably, to save money.

***George Osborne:*** In the aftermath of the financial crisis, to show that the country was getting a grip on its public finances—

**Chair:** It caused a lot of havoc for people. Anyway, we will come on to pensions in a minute.

***George Osborne:*** I think a lot of that was to do with the raising of the female state pension age in the 1990s, which was passed through Parliament and widely advertised at the time.

**Chair:** And that was changed at very short notice.

***George Osborne:*** For both men and women.

**Chair:** Yes, but it compounded that first point. Anyway, we will be coming on to pensions.

Q251 **Catherine West:** I have two quick questions: one about national insurance, and one about the national living wage, the London living wage and regional living wages.

On national insurance, there was quite a controversial change by the Chancellor last year, which some employers were very unhappy about, but which, over time, might end up creating more balance or revenue. What is your assessment of that element? Conversely, there is currently a think-tank that is saying, "No, no, we'll do the opposite to spur jobs."

The second question is about the living wage pushing up against entry level. What are your views on how it is slightly abutting on entry-level graduate jobs? The Committee has not taken a view, but it is an interesting point to reflect on for you, who introduced the NLW, and for those of us who introduced the London living wage.

***Sir Vince Cable:*** The national insurance on employers was based on the assumption that employers would pay it, but they do not: it is passed back to workers and it cuts jobs. It was not a good tax. It has damaged business confidence. It stemmed from the unwillingness to raise taxation through the main tax system. One of the main damaging consequences is that it has provided a big boost to the gig economy, because Deliveroo does not pay employer national insurance; it relies on the honesty of the deliverers. National insurance on employers has had all kinds of negative secondary effects.

As for its interaction with the minimum wage, we know from our experience in government that the minimum wage—living wage—is extremely popular: I think we competed with each other at the end of the Parliament to see who could make the best offer on the minimum wage. But I think we now have to recognise that it is in problematic territory. The so-called bite, which is the difference between the highest level of the minimum wage and average graduate income, is now at about 65%. There is now relatively little incentive for people to get a degree or a higher school qualification, and that is a major constraint on pushing it further.

***George Osborne:*** I think it is a combination. In the coalition Government, we actually reduced employer national insurance. One of the things that we would talk about at the end of that Parliament was that more jobs had been created under that Parliament than under any other Parliament in British history. That was against a backdrop of people thinking that unemployment would rise, not fall, because of the financial crash.

The trouble is the combination of three things: the increase in employer national insurance; the rising living or minimum wage, which I am proud that we introduced and as a result of which the incomes of the lowest paid have increased markedly over the last 10 years; and employment law changes.

That is a triple whammy at a time when unemployment is starting to rise and, as we mentioned earlier, when we are potentially about to have an AI revolution that will make it much easier not to employ people when you can get computers to do things instead. We might find in three or four years' time—it could happen as quickly as that—that we have quite a serious unemployment problem, which we have not seen in Britain since I was a teenager, really.

Q252 **Bobby Dean:** We have spoken a little about the OBR. I think you said, Mr Osborne, that the OBR needs to back off a bit; Sir Vince, you said that instead of marking answers, it is starting to set the questions. There has been a lot of talk about the degree of fiscal headroom that the Chancellor has left herself and about how much that is a problem in and of itself, with incessant tax speculation for the past year or so, for example. How much headroom should the Chancellor seek to build?

***Sir Vince Cable:*** George has given a very eloquent description of the political problems with headroom, but in terms of the basic economics, we have had evidence of growing volatility in the big macroeconomic factors that Governments have to deal with. We have the possibility of a big shock that might come; we have had covid, the financial crisis and Brexit, and others might well be coming over the horizon.

There is a big AI boom, which is producing remarkable results for the companies involved. It may indeed produce productivity growth; it may also be a bubble. We could have a very painful correction, with significant effects on financial markets, including ours, and the economy. There is a very powerful argument in principle for having a significantly higher level of headroom than we have at the moment, bearing in mind the politics of how you deal with it.

Q253 **Bobby Dean:** Mr Osborne, may I pick up on something you said about the OBR backing off? By that, did you mean that the Treasury should be allowed to stick to some of its own forecasts, such as what trade deals it thinks will happen or the impact of the planning Bill, and then take the political risk—so the OBR assesses those things and say how likely or unlikely they are, but the actual figures that are turned out are based on company forecasts? What did you mean by that?

***George Osborne:*** No. Let me be clear. The OBR is blamed by the people on the right who want to cut taxes but not cut expenditure to make those tax cuts affordable, and it is blamed on the left by people who want to raise spending and think that that will pay for itself. The OBR does a very good job at telling both that their plans are fantastical.

Partly because of the low headroom under which the Chancellor is operating under, the OBR has got into a daily dialogue with the Treasury about the impact on GDP of other measures that the Government are taking: the Prime Minister's trade deal with the US or India, the immigration White Paper or whatever it happens to be.

If I were the OBR, I would not try to micro-forecast all those broader economic policies, because then you end up with the Treasury. The Treasury is brilliant and I loved working there, but I know exactly what the Treasury officials will be saying, which is, "Let's get them to score the trade deal, and then we won't have to put taxes up on pasties," or whatever it happens to be.

Q254 **John Glen:** May we turn to welfare and pensions policy? Twenty-two per cent. of total Government spending is on welfare. Mr Osborne, you talked about the achievements of auto-enrolment and, Sir Vince, you talked about the issues of the triple lock and that achievement.

A way of dealing with that pressure might be to put a ratchet on the increase from 8%, which is generally seen as inadequate as a total amount of saving on pensions, so that over time, generally, people would be forced to spend more on their pension. We could also put some sort of time limit on the 2.5% ratchet, given that outside the pandemic, in only one year of the past 10 have we seen growth in the economy at above 2.5%. Isn't there room for a quite radical reset in the area of pensions? Do you think the Chancellor would be well advised to do that?

***George Osborne:*** I think increasing the auto-enrolment rate is a very good idea. It is ultimately optional, although people have to opt out of it, and it has been a really successful UK policy pursued by Governments of all colours.

Q255 **John Glen:** But not adequate enough at 8%.

***George Osborne:*** You can increase it; the system has been established. It is now well respected and most people participate in it. The triple lock was a Liberal Democrat proposal in the coalition talks, which we agreed to. It is worth remembering Barbara Castle had been out there campaigning for years. There were big marches around pensioner poverty in the ’90s and 2000s.

This policy did not come out of the blue. It was designed to address a serious problem, which was pensioner poverty. I am not saying pensioner poverty does not exist today, but we are in a markedly better position. Unless you are prepared to go back to an earnings link, at the moment it is the inflation that is triggering the triple lock. That is not a double lock. That is a single lock, going back to the Margaret Thatcher policy of linking the pensions to earnings. If you want to go back to that, the ghost of Barbara Castle will come and revisit this Government.

Q256 **John Glen:** Sir Vince, do you want to come in and say anything different on that?

***Sir Vince Cable:*** In a way you answered the question yourself. If we moved from a triple lock to a double lock and simply removed the mandatory 2.5%, which is way in excess of current or expected economic growth, that would provide pensioners with protection, but it would also put it on a more sustainable basis.

Q257 **John Glen:** Can I ask about the issues of the future liabilities in terms of pensions? We have obviously got some quite big differences in the public sector liabilities going forward. Some opposition parties have been looking at this. Mr Osborne, when you were in government, you introduced the career average imperative. Where do you see scope for reform in this area, given the wide discrepancies now between DB and DC pensions and what that means for our society?

***George Osborne:*** I think you would have to address public sector pay if you were going to get rid of career average DB schemes. You would have to bump up annual pay. Remember, it is an overall package in the public sector, which is often forgotten in the pay negotiations, but they have got more job security and they have pensions. That is not the first thing I would look towards, to be honest, now that you have got the career average schemes.

Personally, I did not really see the point of the last Conservative Government getting rid of the limit on lifetime pension savings, which I had brought down. The reason they did it was because you run into problems with DB schemes for consultants, judges, senior military officers and, dare I say it, members of the Government. But I think they can be addressed somewhat separately because—

Q258 **John Glen:** I recall looking into it in some detail as Chief Secretary—

***George Osborne:*** I know it is very complicated, but if you are looking for ways to save money, I did not think it was necessarily the right—

Q259 **Chair:** Do you think Chancellors should do things to pensions at the Budget rather than in a long-term approach? Let us take the lifetime limit, which you introduced. You focused on it for a bit while you were Chancellor, then you stopped being Chancellor and no one uprated it. Then it hit these problems. In 2012 in the Public Accounts Committee we were picking up that people were leaving jobs because it was not worth their while working. Doctors and so on were retiring early because they could afford to. Nobody really kept an eye on it and then we hit these big problems.

***George Osborne:*** I think it was more like the tail wagging the dog, because it was particular problems in public sector DB schemes where notionally there is a very large pension pot. Of course it does not actually exist. It is funded out of current taxation and it hits the lifetime allowance. But the last Government got rid of the lifetime allowance, so wealthy people can put a lot of money into pensions again. In terms of pension reform, I would argue that the pension reforms we introduced were successful in 2013-14. Ruth Kelly's pension reforms were pretty effective as well when I was in opposition.

Q260 **Chair:** But at the Dispatch Box, on Budget day, think of the whole of Government accounts, which lays out everything, although it does not include pensions. And then you have got the Budget—you talked earlier about the rabbit out of the hat at the end. Is that the right place to make pension policy, because of the other political pressures on the Chancellor?

***George Osborne:*** I think it has to be balanced; ultimately, you have to put all these things into the mix to make your sums add up. Other aspects of pension policy, such as pension age, require separate legislation and separate debates, but if we are talking fundamentally about the taxation of pensions then the Budget is the tax event.

Q261 **John Glen:** When you were Chancellor, you looked into Michael Johnson's proposal on the lifetime ISA, which was characterised as an attempt to create an alternative savings vehicle. Given that £10 billion to £15 billion of pension relief is on higher rate taxpayers and that, if you had had mass adoption of that vehicle, you would have had different levels of tax relief, is that something that you think is still unfinished business?

***George Osborne:*** Yes. If I was given a ninth Budget, I would definitely have done that. People understand ISAs. A precursor was introduced by John Major, but Gordon Brown introduced ISAs and we increased the limit to £20,000. They are very simple to understand. Pensions have got unbelievably complicated for people, certainly outside the public sector, and most people, even very financially literate people, do not really have a clue what their pension pot is. There is an idea that you could essentially replace pensions with ISAs as a vehicle for saving, so that things are tax-free on the way out rather than tax-free on the way in.

I was very tempted to try to do that. This comes back to your point, Chair: sometimes in Budgets, the rabbit out of the hat does work. With the sugar tax I introduced, if I had announced a sugar tax in advance and consulted on it, it would have been killed by the industry and lobbying forces out there. But it was done as a surprise in a Budget, so by then it is already happening and people are reacting to it. On the pension changes, I made what in hindsight was the mistake of consulting on them, and the pensions industry went mad and I had to back off.

***Sir Vince Cable:*** I do not have a great deal to add. One of the great difficulties we had in the coalition—maybe George is too modest in not acknowledging it—was that, when we did try to push through public sector pension reform, there was widespread industrial action. It was one of the most controversial and difficult things we had to do. It did partly address the problem you describe and, although it was not ultimately a matter for the Government, one of the difficulties was persuading Members of Parliament to accept more restrictive—

***George Osborne:*** And judges.

Q262 **Chair:** You had advice from the Treasury that it could break the law, and then the McCloud case obviously threw that up.

***George Osborne:*** I am receiving lots of letters about McCloud now, as an ex-MP.

Q263 **Chair:** It created chaos for people; some people who have to make decisions will not make them until their point of retirement, so it is keeping parallel systems running, with huge costs to those pension schemes.

When you are making a Budget, there are decisions you could make in one Budget that can have long-term ramifications. I call them "the George Osborne ticking time bombs", because there are a few like it; we will maybe get to those if we have time at the end, but this was one. Were you aware of that in the heat of the 4,000 decisions you were trying to make on the Budget?

***George Osborne:*** I think public sector pension reform was done more across the Government. Certainly it was driven by the Treasury wanting to get it done, and the subsequent McCloud judgment and problems did not come up at the time, or else—

Q264 **Chair:** But you had some warning that there would be a problem about equality law on this? It was warned at the time.

***George Osborne:*** Not that I recall. Mainly it was me and Len McCluskey in my office having lots of rounds of negotiations. We dropped the auto-enrolment in the Labour party in return for him agreeing to career average pension schemes.

**Chair:** We learn something new every day.

Q265 **Bobby Dean:** This has been mentioned already, but with state pensions and public sector pensions coming from general taxation, this feels to me like a big and increasing forecasting problem for the public finances in the long run. Should we be getting the OBR to independently review and forecast what that liability looks like? Should we be doing anything more radical than that? Or do we just keep dealing with the fact that we need to pay for these out of general taxation on a year-on-year basis?

***Sir Vince Cable:*** I think that, as part of the more general oversight that the Chair has alluded to, trying to deal with pension issues piecemeal and particularly in a Budget is not very helpful, and trying to get a cross-party deep analysis, whether it is done by the OBR or some other body that has more people—the OBR is actually quite a small organisation—seems to be a secondary issue.

Q266 **Bobby Dean:** Some form of independent review?

***George Osborne:*** The independent review is a much underused device these days. Again, trying to be unpartisan, I would say the Blair-Brown Government used it pretty successfully quite often, and we used it. It is a way of trying to create parliamentary consensus.

Q267 **Chris Coghlan:** Mr Osborne, in the spring statement, the Chancellor was able to upgrade GDP by £11 billion a year, using the uplift in defence spending, based on a fiscal multiplier of 1.6. That comes from Paolo Surico on how you can use defence R&D to raise economic growth.

I say that because on the way in here I listened with interest to your podcast on the debt doom loop, which I think you did back in July, but isn't there potentially a third way in terms of that challenge around fiscal constraints? Europe faces a fundamental strategic challenge. With the disengagement of the US and with Russia, we all know it needs to increase defence spending.

If Europe issued debt, pooled debt, to raise defence spending, you use the fiscal stimulus from that to boost economic growth and you don't spook the bond markets because you do it in conjunction with our European allies, you could therefore deliver a fiscal stimulus and perhaps help partially offset the doom loop that you suggest.

***George Osborne:*** I think it was my fellow podcaster on *Political Currency*, Ed Balls, who said that the Government did have an opportunity, earlier this year, to come off its fiscal rules or create an additional fiscal rule saying that because of the defence threat from Russia, you could borrow outside the rules. Of course, the German Government essentially did that. Ed Balls judges and I would judge that today that moment has passed somewhat for the UK and for this Chancellor. The bond market is, I think, sitting more heavily on her shoulders, and that moment, that window of opportunity, has passed.

It is quite a crude fiscal stimulus. I think, originally, John Maynard Keynes said that defence spending is not your ideal fiscal stimulus, because you are trying not to use the things you are building—your missiles, artillery shells and so on—but you are right that it can certainly spur innovation. I referred earlier to my role at Stanford, and Stanford was partly built on the back of US military spending and innovation. I would say the single biggest challenge in this space—not for this Committee so much—is the innovation you want to be encouraging. I would fear that increases in defence spending at the moment are going into cost overruns on old programmes like frigates and armoured cars, rather than the very different battlefield we see in Ukraine.

***Sir Vince Cable:*** If we are talking about defence and how to manage defence spending in an economically useful way, I will refer to the work that has been done on the industrial strategy. One of the biggest reasons that persuaded me and, I think, my colleagues to adopt an industrial strategy in the coalition was what was happening to the British aerospace industry, which is at the heart of defence procurement. It was disappearing: without Government's 50:50 funding of R&D, much of the industry and its supply chains would have simply disappeared. This Government has introduced an industrial strategy. It has been quite quiet about it, but this should be very much at the heart of it.

But simply using defence spending as a stimulus is questionable. I remember that when we were debating plan Bs in the coalition, the IMF produced a report on how you give the best stimulus to the British economy. I think the Keynesian multiplier for all forms of public spending and tax cuts was about zero, but public investment was significantly higher, and if you are trying to stimulate the economy, that is probably where you should be looking.

Q268 **Chris Coghlan:** Defence R&D is a form of public investment, but more broadly, you said earlier that the Chancellor was getting it right in terms of increasing public investment. Do you think that the Government is putting enough money into public investment? I am thinking particularly of the cuts under the coalition.

***Sir Vince Cable:*** Historically, Britain has a relatively poor record in investment both private and public. One of the problems we have battled with over the years is the Treasury orthodoxy that public investment is a waste of money and inevitably crowds out private investment. I think we demonstrated that that is not correct. You can have sensible forms of public investment.

The industrial strategy work on co-financing the automobile industry and aerospace is a good example of that. One of the best examples was the green investment bank that we set up. We got £2 billion from the Chancellor and it leveraged another £10 billion from the private sector. It was co-financing. For some reason, George's successor decided to get rid of it. There are many instances like that where properly deployed public investment can stimulate private investment rather than replace it.

Q269 **Chris Coghlan:** Mr Osborne, do you think the Government have the right approach to public investment? Should they be increasing it or putting it in different areas?

***George Osborne:*** I thought the Chancellor was quite smart in adjusting the fiscal rules at the last Budget to allow for the new definition of public investment, taking into account net assets. You could have presented an alternative Budget last autumn that might have had a more positive reaction. Taxes were raised.

If the Government had spent more of that money on infrastructure and investment in the economy, I think the markets would have reacted more positively than they did. If you follow the bond market while she was giving her Budget, it is when she announces that the money is going into current NHS spending that the bond market goes, "What are you up to?"

In this Budget, if I were her, I would return to the thesis of, "I am borrowing money to invest in R&D, infrastructure and the like" and make more of that than they currently do. In the speech yesterday, growth and public investment did not feature as one of the priorities for the Budget.

Q270 **Chris Coghlan:** Given what you have just said, and what you said earlier about US productivity greatly increasing relative to the UK and Europe, do you think the lack of public investment under the coalition was part of that issue?

***George Osborne:*** I will not get back into all the arguments from the time. We thought we were increasing public investment off the plans that Alistair Darling had left us and made a big deal of that, but it was an overall reduction. We were saying, "We are doing more than the Labour Government were going to do", but the overall impact was a reduction in public investment as part of an overall reduction in public expenditure after the financial crash.

There are things like road schemes that we came back to. We cancelled on arrival the A303 Stonehenge tunnel—

**John Glen:** Shocking!

***George Osborne:***—through John Glen's constituency, or nearby, and reinstated it two years later. Then Rachel Reeves cancelled it in the first month as Chancellor.

**Chair:** It has been back and forth like a yo-yo.

**John Glen:** The traffic jams continue.

***George Osborne:*** There are definitely yo-yo things. Generally, as Chancellor, the frustration was a lack of big projects to invest in. I was demanding, "Where's the trans-Pennine rail link we can invest in? Where's Crossrail 2?" On the very first day I was Chancellor, the Treasury said, "Why don't you cancel the Elizabeth line? It's not built yet and no one's going to notice it not being there." Every time I travel on it, I go, "Thank God we didn't cancel the Elizabeth line."

Q271 **Chris Coghlan:** You made a very interesting point about the lack of projects to invest in. Given the negative real interest rates you experienced at the time, was that a key missed opportunity to invest, or was it more a lack of projects?

***George Osborne:*** We tried to course correct in the middle of the Parliament on some road schemes that we had cancelled and then reinstated, some of which have been built. Without getting into it, John Prescott cancelled a load of road schemes, Alistair Darling reinstated them, and then I cancelled them and reinstated them, and then they got cancelled. If you were looking for longer-term decision-making, you could try to get some parliamentary consensus on road schemes, or indeed rail schemes like HS2, where you need long-time horizons. There have been seven Chancellors since me, and you cannot have every Chancellor cancelling the thing that the last person did.

Q272 **Yuan Yang:** To add to the point about capital, Mr Osborne, you mentioned in an interview that you regret the amount of capital cuts that you made during that period. You just mentioned that you attempted to course correct. Why was there the attempt to cut capital spending at a time when interest rates were almost zero, so you would have virtually free money for the Government to invest?

***George Osborne:*** We were essentially operating off the base line that we inherited from the late Alistair Darling, and he had built in plans to cut the deficit, which at the time was 11% of GDP. He had a big cut in capital spending, and we in the coalition said that we were doing better than what we had inherited. Of course, with the passage of time—

**Yuan Yang:** But that is not what residents will feel.

***George Osborne:*** Of course, but with the passage of time, you look back on it. This is a challenge that is easier to see when you are outside Parliament than when you are in it. At the time, you think you are doing one better than the people who came before you, and you are outfoxing your political opponents. However, you then take a step back and go, "Well, maybe that just was the wrong thing and we should have totally rethought the capital budget." We definitely cancelled some things that we had to reinstate later, or wanted to reinstate, which obviously was not ideal.

Even if we had massively increased the capital budget, it would have put more pressure on current spending at a time when we had such a high budget deficit, and it would also have meant more pressure to raise taxes. On the borrowing, it is all very well to say, "Zero interest rates" or "negative interest rates." At the time, a lot of our European neighbours were in fiscal crises, including Greece and Ireland.

Q273 **Yuan Yang:** We were not in the euro at the time.

***George Osborne:*** Yes, but the Liz Truss and Kwasi Kwarteng mini-Budget, and this Chancellor's experience in the last year—once when she was doing the Budget and once a couple of months ago in Parliament, when it looked like she might quit—shows you how close Britain is to the market suddenly taking a different view.

**Chair:** I don't think she was looking to quit, just to be really clear.

***George Osborne:*** No, but the market thought that she might.

**Chair:** I just wanted to be clear for the record.

***Sir Vince Cable:*** This is something that we had quite a lot of strong internal argument and debate about in the coalition: why we could not borrow at low interest rates for investment. The answer George has given, and the advice that we were getting from the Treasury and our economic advisers, was that the bond markets do not distinguish between capital and current spending—it is all borrowing. That was the argument that was thrown back at us. With hindsight, there are many things that the coalition did in fiscal policy that I strongly defend, even though they are unpopular, but this is one area where, with the benefit of hindsight, we could have taken a different track.

Bear in mind the specifics. The one big public investment that was in front of us was HS2—I think it still accounts for half of public sector spending. When it came to our Cabinet, the benefit-cost ratio for HS2 was about 1.6, which is barely credibly, and the subsequent Government decided to do the low-value part of the project rather than the high-value part. We were not dealing with this in abstraction; we were dealing with real-world problems in borrowing, and in that there were a limited range of projects, of which that was the biggest.

Q274 **John Glen:** Can I turn to Brexit, trade and tariffs?

***George Osborne:*** My favourite topic, Brexit.

**John Glen:** Previously, at last year's Budget, the Chancellor did not mention Brexit as a cause of productivity performance, yet in the last few weeks, and in her speech yesterday, she has done. Why do you think that is?

***George Osborne:*** It is the word that dares not be mentioned by British politicians, or it has not been mentioned since 2016, for different reasons. There has been a kind of conspiracy of silence in British industry, the trade union movement and everyone else not to talk about the very obvious—to the rest of the world—damage that Brexit has done. That is not to relitigate the referendum; it is to say that you could have left the European Union in a very different way with much less economic damage. Indeed, at the time, there was a strong argument from some Brexiteers that we could have stayed in the single market and the customs union.

Q275 **John Glen:** Should she look to rejoin those now?

***George Osborne:*** I personally thought that the Labour Government should have rejoined the customs union on entering office. That would have put the Opposition in an impossible situation today of saying, "Elect us, and we are going to come out of the customs union." Good luck trying to get elected on that platform. But they did not. I strongly applaud what the Prime Minister and others are doing to negotiate a better trade deal with the EU, and I would urge them to double down.

To come back to my point about the levers on the desk, building a railway is going to take 15 years. Negotiating a better trade deal or services agreement with the EU is something within your gift—and the gift of the European Union negotiator, so it is not just yours, but it is something that can be done by Ministers and by Governments. We all want to improve skills in the economy, the transport system, healthcare, and we want to help people on sickness benefits. Those things are urgent, but they are very difficult to manage in large and complex democracies. Negotiating a better trade deal with the EU could be done in a matter of months.

Q276 **John Glen:** Given what you have previously said about the shift in growth in the US compared with the EU, how do you reconcile the enhanced opportunities that you would say exist from rejoining the customs union and the single market with the fact that the shift in productivity in the top seven economies is coming from the US, not from the EU?

***George Osborne:*** What no one says is that Britain's absence from the European Union has made the European Union in some ways less dynamic. The British voice is not heard when devising things like financial services regulation in the EU, so I would say that the EU has missed Britain. Many small and medium-sized businesses in your constituencies have given up exporting to the continent of Europe—it is just far too difficult—so there is still a physical trade in goods that you can improve dramatically. The fact that Europe collectively, ourselves included, have not got our act together in terms of productivity vis-à-vis the US over the past five, six or seven years does not mean does not mean that we cannot try to do so going forward.

These are all reasons why we should co-operate with our largest trading neighbour without rejoining the European Union and reopening the debate on free movement. If I were running this Government, those are things that look to me like pretty easy wins, quite straightforward things to deliver and—using my old hat, as someone who ran two general elections—to trap the Opposition.

Q277 **John Glen:** Thank you. Sir Vince, would you like to add anything?

***Sir Vince Cable:*** I think my position on Brexit was always fairly clear. I do not want just to rehearse all those arguments, but the Office for Budget Responsibility has now pulled together the empirical evidence, which suggests that the cost to our GDP is even worse than some of the more pessimistic predictions. I think we are talking about GDP being 5% less than it otherwise would have been, and that probably excludes the damage to business confidence, because there was a very sharp fall in business investment immediately after 2016. The Government's own impact assessments show that the total value of all the bilateral trade deals that we have signed, including with the United States, are the equivalent of adding about half of 1%, so we have gained one tenth of what we lost in crude quantitative terms.

To your point about the United States, there is an obvious desirability in remaining close to the United States in economic terms, but the agreement we have reached was essentially about mitigating the cost of tariffs. It was not about improving market access. As far as I know, it is not a treaty; it is a provisional agreement. One of the things that we gave up in the process was our technological sovereignty—it involved us accepting that we cannot tax or regulate big tech companies, which was an extraordinary thing for the Government to have conceded.

To finish on a positive note, George suggested some of the things that the Government ought to have been doing or could be doing. I would add that the annual process that has now been set up seems to be a very positive step. It gives a means by which business groups and others can bring forward concrete proposals on particular aspects of regulation that need to be aligned. So there is some light at the end of this tunnel.

Q278 **Bobby Dean:** Sir Vince, you say that the value of these free trade deals is worth 10% of the deal that we had with the European Union. Is that in net terms? Obviously, the EU is free to negotiate trade deals with all these other countries as well. Are you saying that one of the freedoms of Brexit means that we have been able to get those trade deals over and above the value that the European Union can strike, or are you just saying in isolation?

***Sir Vince Cable:*** The European Union has itself reached agreements with, I think, Mercosur, ASEAN and potentially India, which we would have been able to take advantage of had we remained in the European Union. I think that the measurements of the last Government were gross rather than net, but I am not sure exactly how they did their calculation.

Q279 **Chris Coghlan:** Do you have any regrets about the policies that you implemented in coalition? Are there things you would advise the Chancellor to do differently?

***Sir Vince Cable:*** I do not regret going into the coalition; I think it was forced on us by circumstances. There were quite big ideological differences, which were genuine and which we had to reconcile, but the political facts in 2010 did not leave us with any other option. The fact that there was a major financial crisis in the background meant that we had to act responsibly. I am glad that we entered the coalition; I think it was the right thing to do.

The Government did a whole lot of very specific things that I was uncomfortable with, but we were all in that position. Although people quite rightly pick on particular sectors—like the justice system and the police, which have suffered particularly badly over a long-term period—I would also point to some of the quite courageous things we did on public spending, which subsequent Governments have not been able to do. A good example was the aid commitment—the 0.7%—which we upheld. The fact that this Government have walked away from it, like the last one, is doing a great deal of damage to our reputation and our national interest. There were positives and negatives—I could give you lists of both.

Q280 **John Glen:** On that point, the world has changed quite considerably. Our Prime Minister is not sat having a pint with the President of China any more. The world, defence and the risks facing the country are different. Are you really saying that, if you were in office now, you would be able to maintain aid expenditure at that level?

***Sir Vince Cable:*** Well, we might have had to change the focus, but the principle was right. The aid budget is not being used for alternative foreign policy reasons. It is being used to support the asylum hotels. That is just a bit of rather cheap public accounting. We were under very strong attack at the time—a lot of George's Back Benchers absolutely hated it—but it was something that we kept going. I would add, because it was my own personal bailiwick, that we put a substantial amount of financial commitment behind our industrial strategy, although there was an opportunity cost to that: a lot of people would have said that, instead of supporting the car or aerospace industry, you should be increasing benefits here or there. We did make some difficult but right choices.

**Chair:** You were also bound into decisions because of the quad arrangement, weren't you? You had to stick to things. You could not just change.

Q281 **Chris Coghlan:** I want to ask the same question to you, Mr Osborne. I am particularly interested in the decision to dismantle Sure Start, if you could cover that in your answer.

***George Osborne:*** I echo what Vince said about the coalition. Obviously I am extremely parti pris, but I think people might look back on that as the last time there was a stable Government with a clear plan, which, whether you liked it or not, they got on with. There were also some very major public service reforms during that period.

I would say that the education reforms were one of the great achievements of that Government and have led to marked improvements in English school standards. Unfortunately, you can compare them directly with Welsh and Scottish school standards to see that there probably was a difference in the way that English education was handled during that period compared to the rest of the UK.

On early years, I think that is an open debate. I am not sure that shiny new Sure Start centres popping up everywhere were necessarily the best investment in early years. There was a big commitment on nursery education, which has been built on by the Sunak and Starmer Governments.

Apart from the political regret—I suggested to everyone involved that we fight the 2015 election as a coalition, but no one agreed with me—healthcare reform was a massive missed opportunity. The healthcare reforms sucked the energy out of returning to NHS reform, which basically no Government since has dared return to—although arguably Wes

Streeting's abolition of NHS England is the first attempt in many years to do that. That would be one missed opportunity.

Without getting too technical, I did not go back into the banking system because Alistair Darling had done a lot of the heavy lifting there. In fact, RBS was heavily impaired. For the first two years half of all small businesses in Britain had an account with RBS. It was still basically squeezing its balance sheet and there was a credit crunch on. It took us two years to reopen the deal on RBS.

Finally, you talked about my first Budget, but during my last Budget a member of the Cabinet resigned on me because I tried to curb incapacity and disability benefits. That was the last attempt, until this year, where a Government have really tried to do that. As you see from Charlie Mayfield's excellent report today—which has lots of great things in it about what you can do to positively support people in the workplace—you have this ballooning bill, which is going to squeeze out all the other things you will collectively want to do as parliamentarians.

Q282 **Yuan Yang:** Mr Osborne, you mentioned that you do not regret scrapping Sure Start because there could have been other investments in early years that would have been more effective. Did you make those other investments?

***George Osborne:*** We made investments in or extended free nursery education. We also introduced free school meals for the first three years of primary school.

Q283 **Yuan Yang:** And you felt those were more effective than keeping Sure Start?

***George Osborne:*** On Sure Start, I would note that there is a Labour Government. If they want to reintroduce Sure Start, they can.

**Dame Siobhain McDonagh:** That goes against everything you spent the last two hours talking about.

Q284 **Yuan Yang:** Would you propose that this Labour Government continue with its plans?

***George Osborne:*** Certainly, I think investment in early years is a good thing, and anything you can do to make childcare—

Q285 **Yuan Yang:** That is not what you did at the time.

***George Osborne:*** We did invest in free school meals and free nursery provision for parents. That was more about putting the money into the hands of parents to get more affordable childcare. The evidence at the time on Sure Start was mixed—I know that there has been work since. As I say, it felt at the time that a lot of the money had gone into big new buildings, which is not always the best use of public money.

Q286 **Yuan Yang:** Was there evidence given to you at the time by the Treasury or other Departments about the cost-effectiveness of Sure Start?

***George Osborne:*** It was generally felt at the time that it had not been very cost-effective.

Q287 **Yuan Yang:** It was generally felt, but was there evidence, because you just referred to evidence?

***George Osborne:*** I do not have perfect recall. I am happy to come back to the Committee, but I do not remember everyone saying, "This is really working well, and we shouldn't get rid of it." Otherwise, if you think about the time, there would have been a big political obstacle to getting it done—which there was not.

**Yuan Yang:** I think the families who used Sure Start would have felt differently about that, but let us zoom back.

Q288 **Chair:** You talk about putting in nursery education, but Sure Start was a lot more than that because it involved health and parental support. If you look at some of the impacts we are seeing now on young people—the high number on PIP having been on DLA or EHCPs—there is a whole trend of young people who have not had support. The long-term cost to the Exchequer is enormous.

You have not touched on welfare. In the rush to make the changes for the Budget that year, were you thinking about the long-term impact on that, or was it something that was just not a concern?

***George Osborne:*** I think at the time it was felt that it was overly focused on quite capital-intensive new Sure Start centres.

Q289 **Chair:** They weren't supposed to have desks. I do remember that people got desks a bit more than were supposed to be out there, but that could have been resolved, could it not, without actually scrapping it?

***George Osborne:*** As I say, I think overall the education reforms and the investment in free nursery education and the investment in free school meals were positives in that space and have been borne out by educational results, which presumably also reflect people's early years.

Q290 **Chris Coghlan:** Are you worried at all that the scrapping of Sure Start, with all the evidence that early intervention is very effective in terms of childhood outcomes, combined with the education reforms that, absolutely right, raised educational standards as a whole, but had an increased focus on test taking, may have harmed the children less able to cope with that—that the combination of those two may have contributed to the special educational needs crisis that we are facing now?

***George Osborne:*** I am not sure it is connected to the rapid increase in the number of children being designated as having special needs.

Q291 **Chris Coghlan:** Even though in 2010 there were 1.6 million special needs children and there are 1.7 million now?

***George Osborne:*** I think there are also incentives in the welfare system that drive the classification of children.

Q292 **Yuan Yang:** I want to zoom out a bit more. We are talking about the regrets of the 2010s, and I was at university during the 2010s.

**Chair:** A young Parliament!

**Yuan Yang:** We can go into many different regrets in that stage of my life, but I was studying economics during the coalition Government and I want to return to the topic of growth that we discussed at the beginning.

At the time, the accepted orthodoxy of the economics department was that a desire to run a surplus budget at a time when the economy was under capacity recovering from the financial crisis, and interest rates were very low, would be leaning in the opposite direction from promoting growth and the recovery back to the equilibrium output. So, Mr Osborne, do you feel that your attempts to run that surplus undermined the growth and the recovery?

***George Osborne:*** Well, we ran a deficit, albeit a reducing deficit, throughout the time I was Chancellor. And we slowed the growth of debt because we were reducing the deficit.

I think there are two things. We now know, but it was sort of obvious at the time, that a financial crash, which thankfully, historically, has happened every 60 or 70 years, is an enormous shock; I think you can identify a lot of what has happened in Western politics and Governments with the impact of that shock. We were in the immediate aftermath of that. This assumption that you could immediately bounce back to pre-shock levels of growth was unrealistic and there is no historical precedent for that.

Secondly—Vince has alluded to this, I have alluded to it and frankly the last three years of British politics has been a salient reminder—we were sitting in a situation where we just did not know whether the bond market would lose confidence in the UK in the way it was losing confidence in some of the eurozone countries. We had to make a loan as a country to our near neighbour, Ireland, at that point. Spain was in trouble, Slovakia was in trouble, Greece was in trouble and so on.

It was not obvious that Britain was insulated from those changes, and we were running a budget deficit of 11% or 12%. He is not here to defend himself, but the truth is that in the conversations I used to have with Alistair Darling he was also very aware that this was a really difficult situation. If you read his memoirs, he actually says, "One of the things I would have done was put up VAT," which at the time his Prime Minister screamed blue murder about.

Q293 **Yuan Yang:** At the time did the Treasury, which I presume had the similar mainstream orthodox view of macroeconomics that academic economists had, warn you that attempting to run a contractionary Budget would delay the recovery in itself?

***George Osborne:*** No. If anything, the Treasury orthodoxy was that we needed to go further because, I think, they also thought that we would not have the political will in a coalition Government. It was a hung Parliament for the first time since the 1970s and a coalition for the first time since the second world war: people did not believe that this Government was going to be able to do anything. They thought that the coalition would fall apart or be paralysed, but in fact, working with Vince, Nick Clegg, Danny Alexander and Ed Davey—a welcome member of the Cabinet I was part of—we made big decisions.

It comes back to the point I made earlier: plan beats no plan. If there was one piece of advice I would give the current Chancellor, it is that that is not a bad motto.

Q294 **Yuan Yang:** By 2015-16, central bankers were also coming out not to directly criticise but hint at problems with this monetary fiscal settlement. Central banks had been trying to lean against the impact of a contractionary Budget. For example, in 2016 Mark Carney warned that the Bank on its own could not lift growth off for the UK economy. Andy Haldane, the chief economist at the time, has had much more direct criticisms of your contractionary policy. Do you reflect on those interventions?

***George Osborne:*** Both Mervyn King and Mark Carney subsequently spoke to me. Remember that this was not nearly as tight or contractionary, as you put it, as what almost all European countries were running this at the time, and indeed the United States of America. They talked of fiscal stimulus under the Obama presidency, but the truth was that state governments were running contractionary fiscal policies across the United States. In fact, the fiscal path of the UK and the US was almost identical during that period, if you look back on it.

The Obama Administration and Larry Summers were talking about fiscal stimulus, we were talking about austerity—or you know, getting the public finances in order—but in fact we followed a pretty similar path and it was milder than a lot of European countries were forced to follow.

I stand by the results: the fastest recovery of any of the G7 economies; the most jobs created of any Parliament in British history; and incomes of the poorest 20% rising faster than they had in the previous 10 years. There are lots of things I would have liked to have done more with, but unfortunately this country had a vote on the EU.

Q295 **Bobby Dean:** I want to take the long-run view as well. We have talked about the bond markets, but they will respond to a variety of economic models, so there is no one pathway—it is just that you need a credible plan. Part of the coalition’s plan was to weigh more heavily on spending cuts than tax rises; I think there was an 80:20 rule—not a strict rule, but that was one of the things said.

Given where we are now, with the social infrastructure and foundations—you mentioned the justice system, policing and there are lots of concerns about the NHS and the welfare state now—if you were to take a 25-year view, would you still make the same decisions? Or would you weigh a bit more heavily on the tax side, to ensure that social infrastructure does not disintegrate? Can I come to Sir Vince Cable first?

***Sir Vince Cable:*** Within the coalition there was not a wide range of disagreement, but I think Conservative colleagues would probably have preferred to lean more on spending and us to take a bit more out of tax. We were talking about 70:30 rather than 80:20.

One of the key factors that produced that coefficient was the fact that, on the Lib Dem side, one of our priorities was to lift the threshold for low earners for income tax, so we were arguing for a substantial tax cut for people on low and middle incomes. In a way, we contributed to that 80:20 mix that you describe.

To the introductory part of your question, can I make a point that I think we have missed a little in the discussion about why Britain has this particular extreme vulnerability in bond markets? There is a mixture of factors. The United States is getting away with far more reckless policies than we would ever have dreamt of, because it has a global currency. We are not anchored in the eurozone. The shift away from final salary pension schemes means we do not have institutions trying to soak up Government bonds in the way the Japanese have. We simply do not have the options that many other countries do to manage external public borrowing, and we are therefore particularly vulnerable.

Q296 **Bobby Dean:** Mr Osborne, do you want to respond to that point about the 25-year view of social infrastructure, and whether we are weaker now because we leaned too heavily on public spending cuts?

***George Osborne:*** I do not think that was the case back in 2010 and 2015. What I would generally say is that you do not have to run such a tight policy in peacetime, if you like—outside of the aftermath of a financial crash—but you do need to require reform in return.

Look at the justice system. I keep hearing that it is all to do with money and inputs, but I think anyone who has experience of the court system could legitimately ask it, the legal profession and the judiciary whether they might reform the way they handle themselves, in return for money. If I were the current Government, I would do more striking of deals: "We'll invest in return for reform." In the most successful period of the Blair-Brown Government, they were demanding reform in return for additional public expenditure.

Q297 **Catherine West:** Boris Johnson introduced a hard Brexit but left a legacy of a 1-million-person newly-arrived community, in migration terms, per annum. Would your advice to the current Labour Government be to seek entry into the European Union again?

***George Osborne:*** No. Sadly, I do not think that we can rejoin. I do not know why, as a country, we have decided to swap European immigration for rest-of-the-world immigration, but I was not in the Government at the time.

***Sir Vince Cable:*** Rejoining tomorrow is not an option. In the very long term it may well be and it probably would be desirable, but it will be a fundamentally different organisation. If Ukraine is a member in 10 or 15 years' time, we would be joining something quite different, which probably will have different member states with different sets of obligations and a much more flexible system than we had.

I would like to see us rejoin but over a very long timeframe with a much more open-minded approach.

Q298 **Catherine West:** Your former colleague from Surrey Heath, Mr Gove, said publicly that his biggest regret was cutting the Building Schools for the Future programme. What would yours be, on reflection?

**Chair:** Mr Osborne, you have been quite bullish about the positives. Was there anything you regretted?

***George Osborne:*** I think that the healthcare reforms were a mess. That is such a big area of Government spending and it basically frightened us off ever returning to it. It is annoying. The Labour MPs on the Committee have such a rare opportunity: you have won an election, you have your majority, you have not been in office for a while. This is the moment to be doing the things that are difficult to do. Healthcare reform is the kind of thing that you can only pull off in the first couple of years of a new Government, and that was a mess.

***Sir Vince Cable:*** Certainly, in our time there were reforms that were not exactly stellar. Probation reform was probably the worst example. I had the hospital pass of dealing with universities. I did not expect to be dealing with universities in Government, but I inherited the problem.

We were faced with a situation not totally dissimilar to today. We had a substantial number of universities going bankrupt. If the Government had simply applied the same public spending controls as we had on other bits of Government, large numbers of universities would have had to cut Departments, cut staff and probably, overall, cut fairly drastically the number of students going to university, so we had to find another mechanism.

The unpopular but necessary step that I had to take was to substantially increase the fee level under the system that the previous Labour Government had introduced. That has kept the universities solvent and expanding for 15 years. Of course, they are now back to the same situation that we inherited, but I think that the approach that we adopted was the best of some horrible options.

***George Osborne:*** We did try to make a graduate tax work, but we just couldn't. We spent a lot of time inside the coalition—as I think the Brown Government did—trying to make a graduate tax work.

Q299 **Chair:** That needs to be a cross-party decision over the long term. Mr Osborne, you introduced the two-child limit. We had some good evidence last week that said that it has no impact on fertility, one way or the other, whether you have that limit or not. Do you have any regrets, because that policy has definitely pushed children into poverty?

***George Osborne:*** Absolutely not. I think it is perfectly fair to ask people in society in receipt of benefits to make the same kind of choices that most other families have to make about whether they can afford—

Q300 **Chair:** But some people make choices and then find themselves otherwise, as we heard clearly last week. People might have three or four children and be working and everything is fine, but then they are widowed, separated or lose their job, and suddenly they need some support. The social security system—I think we would all agree that there has to be a safety net there. We can argue about how that works, but that safety net is not there for those children when their family circumstances change.

***George Osborne:*** The vast majority of families in Britain have to make choices when they have additional children, given the cost that that will bring. The system that I was reforming back in 2016 had this strange financial incentive at the bottom of the income scale, and that was reflected—

Q301 **Chair:** We have had evidence to say that that is not what makes people have children. I have constituents in very difficult circumstances, and the one area of agency they have is to have that third or fourth child, sometimes for cultural reasons or otherwise. Where was the evidence? Did you have evidence to suggest that people would make family decisions off the back of the benefits?

***George Osborne:*** First of all, it commanded broad support at the time—I think there was quite a lot of Labour support for what we did. At the time, there was certainly evidence that there were mounting financial incentives for families with large numbers of children. That, also, by the way, was deeply resented by much of the rest of the population. Thinking of all the polling I have seen since, it remains a very popular measure. All I would say is that, if it is going to be changed—

Q302 **Chair:** A lot more children are in poverty now, and changing the cap would be the quickest way of getting children out of poverty. Your Government and subsequent Governments of your party oversaw a massive rise in child poverty.

***George Osborne:*** If you look ahead at where the public might be in three or four years' time, an overly generous welfare system might be a big challenge.

Q303 **Chair:** There is a difference between a generous welfare system and supporting children who have no say over their future. Also, given the falling birth rate—not, I think, the situation when you were in power—would you argue that there is now a need for investment in our children, in the ones that we actually have, because immigration is down, or going down, because of Europe?

***George Osborne:*** We can have another discussion about immigration—personally, I think immigration brings lots of benefits to our country—

**Chair:** The point is that we are in a world where we have lost the

European migration—we do not have migrants and we have a falling birth rate. So investing in the children we have might be a sensible economic move.

***George Osborne:*** If you were looking at how to get Britain going again, then investing more in education, less in incapacity benefits, and more in schools, less in all the apparatus of an ageing society would be sensible things to do. If I had the money and I had to choose—this is what Chancellors have to do—between Sure Start and getting rid of the two-child cap or limit, were I a Labour Chancellor, I would put money in Sure Start.

Q304 **Chair:** Okay. I am sure the Labour Chancellor is listening. Sir Vince?

***Sir Vince Cable:*** This is one area where I disagree. I think that the two-child limit, resources permitting, should be one of the highest priorities of the Government. As you say, it is child poverty, a bad thing in itself, but we are also producing large numbers of very young people, five years old, with very stunted development, which has major long-term economic costs. That is something we continue at our peril.

I will emphasise that, on welfare reform, although the Government are looking at this in the Timms review, the working-age population share of GDP in benefit has been pretty constant for about 30 years. There may be particular quibbles about the way invalidity benefits are applied, but overall, we cannot argue that the share of the national economy going into working-age benefits is ruining the country. It is not. It has been very stable.

Within that, I would certainly prioritise the two-child limit, improving the tapers for universal credit and dealing with things like the extreme limitations on, say, eight-hour working before people start losing benefit. That whole thing should be made much more flexible.

Q305 **Chair:** It is worth noting that universal credit and benefits to children often go to families in work—about half, or just over in in some cases.

I want to touch quickly on frozen thresholds and the big debate there. Were either of you were the Chancellor or in the Government now, what would you be saying about the frozen thresholds? The fiscal drag is real. Are you concerned about that?

***Sir Vince Cable:*** Fiscal drag is one of the worst ways. It is politically attractive, because it is relatively concealed. The big choice we had in the coalition—this Government have it as well now—is: do you just allow income tax receipts to rise by freezing thresholds, or do you go for the basic rate?

It is clear that allowing fiscal drag to operate is much the more regressive of the two options, because people on low incomes are dragged into the lowest band and people on the lowest middle incomes are dragged into the 40% band. So I would have a very strong preference for taking the politically difficult decision to raise rates, rather than allowing fiscal drag to continue to operate.

***George Osborne:*** When we were in government, we did the exact opposite: we raised thresholds. That was our big-signature attempt to help the working poor with their tax bill. This was exactly the kind of debate we would have in the coalition. Vince would say, "It makes economic sense to raise the basic rate of income tax," and I would say, "Yeah, but we can actually get away with freezing the thresholds."

We did the opposite, but if you were sitting in the Treasury today—well, I think that if the Labour Chancellor raises income tax rates for the first time since the 1970s, having specifically promised not to do that in the manifesto, it is going to cause real political hardship for the Government. It might make more sense for the very good reasons that Vince has given, but continuing the Conservative Government's income tax freeze looks like a much more attractive option if you are actually putting together a Budget.

Q306 **John Grady:** Sir Vince, the poorest families in Britain faced a double whammy because they lost Sure Start and they got the two-child cap. I am not aware of any academic evidence at the time that showed that the two-child cap would influence the number of children people would have.

**Chair:** And we heard last week that it doesn't.

***Sir Vince Cable:*** I would agree with that.

Q307 **John Grady:** The question is really twofold. First, did the Government take proper account of the long-term costs? Leaving aside the ethics—for me, this is deeply unethical—did they take account of the long-term costs of these two measures, in terms of lost earnings and lost prospects for the cohort of people affected? Secondly, do you think the coalition Government had a sufficient eye on the distributional impact of their policies?

***Sir Vince Cable:*** We did produce distributional impact assessments, actually. They were critical, but we did produce them and we were aware of them. I cannot honestly recall the decision making around the two-child cap.

***George Osborne:*** To be fair to Vince, it was actually introduced by the Conservative Government after the coalition ended. But we did commission a piece of work, at the request of the Liberal Democrats, that asked, "What are the public expenditure cuts that disproportionately affect the upper income brackets as opposed to lower income brackets?"

The three policies that the Treasury came up with were: university fees—jack 'em up more; get rid of free museum entry—not something I am in favour of now that I am chairman of the British Museum; and get rid of free swimming lessons, which had been introduced by the tail end of the Government who had come before us. We said no to all three, beyond what we had already done on tuition fees.

Q308 **John Grady:** Mr Osborne, did you have academic evidence—robust evidence, as opposed to just general say-so—about whether introducing the two-child cap would seriously influence people's behaviour and decisions about having children?

***George Osborne:*** We produced at the time and had internal evidence on the distributional impact of the policy and its impact on child poverty, and we were confident that we could go on reducing child poverty.

Q309 **John Grady:** Mr Osborne, I say this gently, because I do not want to appear rude at the end of a long hearing and you have been very patient with us. Was there evidence about the influence of the policy on people's decisions as to whether to have children? I ask because one of the key points—

**Chair:** We heard last week that it did not make any difference.

***George Osborne:*** It is not that I don't know the answer to the question because I can't recall whether a specific piece of paper came to me around that, but we clearly felt at the time, and it was widely supported across the political spectrum, that there were disproportionate incentives in the welfare system, which is why there was a clustering of large—

Q310 **Chair:** You are suggesting, basically, that people were having babies to get benefits. You are saying there were incentives.

***George Osborne:*** It wasn't so much that they were having babies to claim benefits; it was just that the conversation that many families in Britain have, "Can we afford another child?", was a conversation we wanted all people to have.

Q311 **Chair:** What we heard last week was that people were having that conversation, quite possibly while working, and then something happened in their life and they needed support.

***George Osborne:*** The great thing about there now being a Labour Government is that you can reintroduce Sure Start and get rid of the two-child cap.

**Chair:** Well, there we go—there are some suggestions for the Chancellor. I thank our witnesses, Sir Vince Cable and George Osborne, very much indeed for their time. We have had a canter through interesting memories, good and bad. There are different takes on what happened in your time in government, but we thank you for your time.

Sadly, with Alistair Darling dead, there are now not many people alive who were in your positions and having to make these decisions, so we really appreciate your time.

The uncorrected transcript will be available on the website in the next couple of days, if you want to have a look at that. Thank you to our colleagues at *Hansard* and thank you to our broadcasting colleagues at Bow Tie.