Treasury Committee

Oral evidence: The economic and financial costs and benefits of UK membership of the EU, HC 499

Tuesday 27 October 2015

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Watch the meeting

Members present: Andrew Tyrie (Chair); Mr Steve Baker, Mark Garnier, Helen Goodman, Stephen Hammond, George Kerevan, John Mann, Chris Philp, Mr Jacob Rees-Mogg, Wes Streeting

Questions 1-92

Examination of Witnesses

Witnesses: **Roger Bootle**, Executive Chairman, Capital Economics, **Simon Tilford**, Deputy Director, Centre for European Reform, **Philippe Legrain**, Senior Visiting Fellow, London School of Economics European Institute, and **Professor David Myddelton,** former Chairman, Institute of Economic Affairs, gave evidence.

Q1 Chair: Thank you very much for coming to see us this morning to discuss this intractable and, in some respects, vast subject, which is to try to work out the costs and benefits of membership, in view of the impending referendum. You are all experts vastly experienced in this field, and we are not going to be able to do justice to everything you would like to put on the record, so what I am going to do is ask one of you to speak on each question. If any of you particularly disagree, speak up, otherwise I do not see much point in each of you repeating pretty much agreement or just making clear that you agree with something that has already been said.

I want to begin with an apparently general question. There have been heaps of claims out there, with wildly different estimates, about the effect on GDP of membership depending on whether people are optimistic or pessimistic about Britain's fate following its departure. I just want to go through a few of these and ask you, as experts, whether you think we should give any credence to them. The CBI has come out with the claim, and repeated it recently, that EU membership is worth £3,000 per year to every household. Does that sound plausible, Roger Bootle?

Roger Bootle: I do not think it sounds very likely. The problem with all of the studies that I have read on this question is that they have to grapple with some complete imponderables. The appropriate way to tackle that is to try to quantify things in terms of a range, but to come out with a hard and fast number is verging on the intellectually dishonest.

Q2 Chair: Does anybody disagree with that view?

Simon Tilford: Putting numbers on this issue is very tricky, because we do not know what kind of arrangement—

Chair: You are agreeing.

Simon Tilford: I am broadly in agreement, yes.

Q3 Chair: Can I come to the next one? The Leave EU campaigns claims: "Leaving the EU could make the average UK household £933 better off". How about that one?

Roger Bootle: It is yet another figure. It is plausible on the basis of certain assumptions, but there are three key imponderables. The first one is what sort of trade relationship we are going to have. We simply do not know. The second is what the effect would be on investment, including foreign direct investment. We do not know. The third is the cost of current regulations imposed by the EU and the extent to which we would rescind them were we not in the EU. We do not know the answer to those twin questions either.

Q4 Chair: Other colleagues will come in on various aspects of those questions. I would like to carry on in this vein, just taking a look at these various claims. The Britain Stronger in Europe campaign has recently reiterated a claim made by the CBI that membership is also linked to 3 million jobs. Do any of you agree with this? Is it reasonable to suggest that 3 million jobs are put at risk if we are to leave the EU, or—maybe I am allowing my prejudices to get out—has the lump of labour fallacy not reared its head here, and are we not talking some pretty ropey economics?

Simon Tilford: The 3 million jobs refers to people working in industries that trade with the rest of the EU. There was a figure put about several years ago that 3 million jobs were at risk. Clearly, that is fanciful. We would not stop trading with the EU; even if we traded with the EU under WTO rules, we would continue to trade with them. What they are saying is that it could negatively impact on sectors that employ 3 million people, so I think the CBI is being quite careful with that.

Q5 Chair: They are wording it carefully, but they are giving the public the impression that there are all these jobs at stake. Is there anything you want to add, Professor?

Professor Myddelton: I do not remember us gaining 3 million jobs when we joined the Common Market, so I do not quite see why we should lose 3 million, which is the implication.

Chair: I think I am picking up the general tenor of the panel. I know I am rushing you.

Philippe Legrain: It is not the impact on jobs per se. In a flexible labour market, wages adjust, so it is the impact on pay. If you have lower productivity, you are likely to have lower pay.

Q6 Chair: Let us move on to this point that Roger Bootle touched on a moment ago about the burden of legislation. Some think-tanks have attempted to estimate the burden by adding the costs of the impact assessments associated with EU regulations and directives. On this basis, Open Europe has found that the top 100 EU rules cost Britain £33 billion per year and the Get Britain Out campaign puts the cost of red tape at £120 billion a year. Are these meaningful ways of thinking about membership? Maybe I could have a yes or no to that one.

Professor Myddelton: No.

Q7 Chair: Does anybody feel a burning need to qualify the "no"?

Roger Bootle: Yes, I do. As I said before, the quantification of these things is extremely difficult, but one should make an attempt. There are several problems with trying to value regulation. The answers tend to come in the form of responses from businesspeople, which are typically pretty flaky, and we do not know what regulations we will put in place of the ones that have been imposed on us by the EU.

Q8 Chair: I think you made that point a moment ago. I am not trying to get into the heavily qualified calculations that people might want to think about; colleagues are going to do that in a moment. I am just trying to take a look at these headline figures that have been put out to see whether any credibility should be given to them in public discourse, and I am getting the impression that the answer is no. Philippe Legrain wanted to say something.

Philippe Legrain: If you look at the Open Europe study, of the most costly regulations they identify, the second is the CRD IV package, which is largely transposing Basel III, which Britain would most likely continue to abide by even if it left the EU. Therefore, that is not an additional cost of being in the EU; it is a regulation that we will be bearing the cost of in any event.

Q9 Chair: I was going to come on to that. For those who are not so familiar with this who may be watching this hearing, that suggests that there is a recurring cost of £4.7 billion a year. This is the Capital Requirements Directive, CRD IV, that I am talking about. I presume that is what you are referring to. Do you agree that the UK would be required to have something very similar to

CRD IV in its domestic law irrespective of whether it was in the EU, because of Basel III? Does anybody disagree with that view?

Simon Tilford: This is the problem with many of these things. To reach the figure of £120 billion, they have looked at every regulation agreed in Brussels, attached an arbitrary value to it and then assumed that, were we to leave the EU, there would be no regulation in any of those areas, which is fanciful, because many of the areas would then subsequently be regulated at national level. One would have to go through very carefully and look at each individual regulation and then estimate whether we would put in national regulations to replace the EU regulation. One has to look first at what they are assuming as the cost of the regulation, and then whether we would replace it with national regulation.

Q10 Chair: The counterfactual—what the world would look like if we were out—has been referred to on several occasions. Does this not render the claims made about the effects on the persistent trade deficit very difficult to estimate as well? Maybe I could put this point slightly differently. I will ask each of you in turn: would this trade deficit get worse, stay the same or improve following Brexit? Does anybody want to offer a view?

Professor Myddelton: Do you mean the deficit with the European Union or with everybody?

Chair: The persistent trade deficit with the rest of the EU.

Simon Tilford: Much of the widening of Britain's deficit in merchandised trade and services in recent years has come with the EU, but more particularly the Eurozone, and it is largely a function of extremely weak demand in the Eurozone following the crisis. The imbalance in our trade with the Eurozone will persist so long as our economy is growing robustly and the Eurozone is not. It is largely a product of that imbalance in rates of growth of domestic demand.

Also, there are demographic differences. Our demographics are healthy. We are fortunate to have a relatively young population, whereas much of the Eurozone has poor demographics. Countries with ageing populations tend to save more; those with relatively young populations tend to save less, and that comes out in trade balances.

Depending on what replaced full EU membership, we would continue to run a significant deficit with the EU, or the Eurozone in particular, almost indefinitely, partly because of the demographics, partly because of different potential growth rates and partly because of the likelihood of ongoing mismanagement of the Eurozone. Without a change to the management of the Eurozone, we will not get sustained recovery of domestic demand in the Eurozone.

Q11 Chair: They are very good points, but I do not want to get too much into the detail, because colleagues may decide to press more deeply on all these areas. I am just trying to get a grip on these headline figures and their validity or otherwise, for the purposes of public debate and discourse. I just want to end with one question. Do you share my personal concern that these contradictory statistics that are being used by both the in and the out campaigns risk confusing the public and will leave the public none the wiser in trying to form a view about the decision that they need to take at the time of this referendum? Does anybody disagree with that?

Philippe Legrain: Part of the reason why conflicting statistics are bandied about is precisely to confuse. Having cast so much uncertainty on the consequences of leaving, there would be an economic cost, and anyone who believes in free trade ought to believe the same. Just because we cannot quantify that cost, it does not mean that it is not real, but if you bandy around 50 different statistics you neutralise the economic issue and you can talk about other issues that might be more salient with voters.

Chair: There are some very real economic issues at the heart of all this, which matter hugely to the future of the UK. It is that that we are going to get into in a little more detail with colleagues' questions.

Q12 Helen Goodman: Good morning. I would like to ask you why you think that the UK's balance of trade deficit with the EU has been growing over time.

Roger Bootle: We have heard already from Simon a large part of the answer. That is to say that the UK has been a reasonably rapidly growing economy over the last couple of years. Domestic demand has been fairly strong. By contrast, in much of the rest of the EU, particularly the Eurozone, the economy has been very weak, so the demand for British exports has been weak. Over and above that, Britain's overall trading position—not just with the EU but the overall trading position—has also been questionable for some considerable time. There are parts of the world where our trade balance has been improving in recent years, but the gist of the answer is the one I have just given, which Simon gave earlier on. It is to do with the different rates of growth of demand.

Q13 Helen Goodman: I will ask the next question to Mr Legrain. Do you think that that will continue or do you think it will rectify itself over time?

Philippe Legrain: In what circumstances? If we leave or just in general?

Helen Goodman: If we stay in.

Philippe Legrain: I share Simon's pessimism about the likely future growth in the Eurozone. There are question marks about the sustainability of Britain's recovery, but, assuming the recovery continues and assuming that the Eurozone remains in a mess, that is quite plausible. There are lots of imponderables, not least how the exchange rate behaves.

Q14 Helen Goodman: That is true. You asked whether I was asking about whether we stay or whether we leave. It sounds to me from what you are saying as if you think that the determinants relate to what is going on in the Eurozone and the management of the Eurozone. Do you think our staying or leaving would have any impact on that?

Philippe Legrain: The main determinants of trade flows are the pattern of production in Britain and the pattern of demand in both the rest of the EU and Britain. I do not see the structure of production in the UK changing dramatically in the coming years. The pattern of demand might. One could envisage a slowdown in growth in Britain, in which case Britain would import less. One could also conceive of a miraculous recovery in the Eurozone—I find that implausible—in which case they might import more.

Simon Tilford: We do have a problem with sterling. The trade-weighted value of sterling is excessive. It is above its long-term value. Its long-term value has been pushed up by large periods of overvaluation itself. There is a problem with the real trade-weighted value of sterling, which is to a large extent down, again, to what has happened in the Eurozone. Because the economy is so weak, we are going to see a very prolonged period of very expansionary monetary policy within the Eurozone, a by-product of which will be a weak euro. One additional reason for our trade performance has been a long period of currency overvaluation.

Q15 Helen Goodman: My constituency is in the north-east of England, and we are the one region outside London that has a trade surplus. In assessing the value of trade with Europe, have any of you done any regional analysis?

Simon Tilford: We did do some work at the Centre for European Reform on the regional impact of leaving the EU.

Helen Goodman: It is quite conceivable that the regional impact varies from place to place.

Simon Tilford: Our conclusion was that poorer bits of the UK that depend disproportionately on manufacturing would be hardest hit, because leaving the EU will have the biggest impact on the manufacturing sector, particularly investment in manufacturing and particularly foreign investment in manufacturing, whereas areas such as London that have a hugely skilled workforce and a broad range of industries would be much better placed to ride out the storm. We argued that the north-east would be one of the hardest hit in the UK.

Q16 Helen Goodman: That confirms my intuition.

I want to ask you about why you think exports to and trade with non-EU countries have been growing. It is a mixture of these two things. It is because the emerging economies are growing. To what extent do you think it is because we have had trade liberalisation with those countries? Insofar as it is trade liberalisation, how much of that do you think would have been achieved if we had not belonged to the EU, with its negotiating power?

Roger Bootle: It is overwhelmingly the growth of these economies. You can see that in the falling share of third parties' trade with the EU. If the EU, and particularly the Eurozone, something like stagnates for several years, and then emerging Asia powers along at 7% or 8%, you do not need to be Einstein or even John Maynard Keynes to realise that percentages of world GDP and shares of trade flows are going to shift. That has been occurring now over a very long time. It is not only about the Eurozone, because these countries principally in Asia have been growing fast for a long time, but the extreme weakness of the Eurozone over recent years has accentuated. It is primarily simply about that.

Q17 Helen Goodman: Does anybody disagree with that?

Philippe Legrain: Germany has been lucky, in the sense that it specialises in producing machine tools and capital equipment, just the sort of thing that China and other rapidly industrialising emerging economies have needed at that stage of development. Britain is well placed to benefit as the Chinese economy shifts towards more services-driven and consumption-driven growth. In the context of the visit of President Xi, there are opportunities for financial services and professional services, English-language education and all sorts of things. It is not just about rapid growth; it is also about what the demand of those particular countries is.

Q18 Helen Goodman: In my constituency, there is the UK's last remaining television factory. This television factory imports components from China and puts them together to make tellies to sell to the rest of Europe. They tell me that they can only afford to do this because the Chinese face a tariff barrier into the EU on completed tellies and they do not. All these things—the inward investment, the trade and all these things—interrelate. You cannot say this is simply about this question and simply about that question, but do you have any sense of how much of our exporting manufacturing is of this kind of structure—importing things from outside the EU, putting them together and selling them into the EU?

Chair: It is a very interesting question. If you have estimates, we would like them. If you are not sure of giving them orally, we would be interested to see them in writing.

Simon Tilford: I do not have a handle on what share of our exports is the result of companies investing here in order to get around various forms of tariff.

Q19 Helen Goodman: Are they getting around them? They are taking advantage of an opportunity that is there.

Simon Tilford: There are lots of reasons why foreign companies invest in the UK. It is partly our openness; it is partly that we are not concerned about foreign ownership of our assets; it is partly language. It is quite clear that lots of companies invest in the UK in order to serve the broader EU market, because FDI is, to a large extent, driven by market size, but I do not think anyone has done any work on what share of that investment that is here in order to access the EU market is here because of tariffs.

Q20 Chair: Philippe, have you done any work on this? Rather than a qualitative reply, we are very interested to know broadly the answer to Helen's question, if you have it. If not or if you would like to think about it, come back to us in writing.

Philippe Legrain: I do not imagine it is very high, simply because there are not many high tariffs left in manufacturing. There is 10% on cars and there are a few tariff peaks—

Q21 Chair: Are they not on the areas that peak?

Philippe Legrain: You would have to look into the figures, but given that the UK manufacturing sector is pretty small and EU tariffs on manufacturing are generally pretty low—in fact, they may average something like 1%—I do not imagine it is particularly large. Your constituency's TV company might be one of them.

Chair: I am sorry to rush you, but I think we have got the point. If witnesses have considered views on that, it would be interesting to hear what they are.

Q22 John Mann: Mr Legrain, I did hear you say that Germany was lucky in relation to having machine tools. I would suggest perhaps Germany has been more strategic in its investment than we have in having a machine tool industry.

My question is to all of you, starting perhaps with Professor Myddelton and moving across. Sports Direct, quite a well-known company, employs approximately 2,300 people in Shirebrook in Derbyshire on a former coalfield site that the state remediated for a cost of around £10 million. Virtually the entire workforce is Polish. Virtually the entire workforce has moved to this country, and its age profile is accurately described as under-50s, so people who would often have had families on arrival or since arriving. Is it to the benefit of the UK economy overall that Sports Direct has invested in this way and, using our membership of the EU, imported in this workforce, or would it be more in the overall benefit of the UK economy if Sports Direct, as a British company, had invested the same amount in Poland and drawn back profits into this country? I am interested to know each member of the panel's view on this.

Professor Myddelton: I do not know the answer, but presumably they think they are better off having done what they have done.

Q23 John Mann: That is not the question. I am sure that is the case. The question is the benefit overall to the UK economy.

Professor Myddelton: It benefits the UK economy in a free market to let employers do what they think is most profitable.

Simon Tilford: It is hard to look at this in isolation. One has to look at it in terms of immigration more broadly and the benefits and costs thereof. It is pretty clear that, overall, we benefit economically and fiscally from immigration, though clearly there are some localised impacts. They have not imported people; it is just that those people have applied for those jobs, and I suspect largely because most people in that area are not interested in doing those jobs. It could also be that many of those people they have employed are more productive than sections of the local workforce, and we would have to ask why that is the case. It is not as if they have gone out of their way to import large numbers of cheap Poles; it is just that those people happened to apply for the jobs.

Philippe Legrain: Briefly responding to your Germany point, it is good luck. It is not strategy. Germany has been making more or less the same thing for 100 years. Along comes a Chinese boom that happens to tap into the things they have been making for 100 years. That is not strategy; that is just luck. I would be worried about Germany's lack of flexibility, because if the pattern of demand for its exports shifts, its economy will not be able to adapt.

In terms of Sports Direct, we do not have all the facts to hand, but I get that the premise of your question is that, somehow, the fact that it is employing Poles means that its benefits to the UK economy are either negligible or indeed negative. I would say that clearly it provides benefits to the UK economy. It pays tax. The Polish workers who work there pay tax. Presumably they have been hired because they are most suited to the job. They in turn spend their wages in the economy, which in turn creates demand for goods and services produced by British people, and so on. Although we do not have all the facts, yes, having Sports Direct employing Polish workers in your constituency is good for the British economy.

Roger Bootle: Broadly speaking, I agree with that. It does bring certain benefits to the British economy, but they are probably not very big in those circumstances. If you assume that this activity had not been there and the Polish workers were not there, depending on what assumptions you make about how the economy functions, it may be that the overall level of production and income in the country would be lower, but I do not think that is a particularly good way of looking at this. You have to look at the effects on the income of the indigenous people, and it is not obvious to me that the effect would be that big. In principle, what Philippe has said is correct; there would be other benefits from having this activity in this country, even though the income goes to Polish workers.

Q24 John Mann: It is interesting that none of you have answered the question. The question was: would it have been more profitable for the UK economy if that investment had been in Poland? Let me ask the question in a different, less specific way. One of the dilemmas with the European Union is that it does not have a free and open labour market, because there are very different systems, so people are attracted by the national benefits, be they tax credits, good schooling, schooling at a younger age, a better health service, differential housing values or different housing markets and options in the housing market. There is not full flexibility; there is an ability with a partial flexibility. Is that partial flexibility a fundamental weakness or is it a strength within the EU? In other words, can the EU, in terms of maximising its real strength, only operate properly if there is a truly flexible and open labour market whereby an employer is investing on a level playing field? Clearly, when we are talking about attractions of working in the UK as opposed to attractions of working in eastern Europe, there is not a level playing field.

Professor Myddelton: To the extent that the European Union economy is flexible, that is good. To the extent that it is only partially flexible, that is not so good. I favour free markets and I think they could do better by having a freer market. You may say that is not really a prospect, and I agree; I do not think it is.

Simon Tilford: Britain does enormously well from this. A very high proportion of people who move here are skilled. A far higher proportion of people coming to this country to work are skilled than those people going to France of Germany.

Q25 John Mann: Do you have a regional breakdown of that?

Simon Tilford: That is disproportionately centred on the south of England. The proportion of people who are skilled coming into poor areas of the country is lower.

Q26 John Mann: Do you have any statistics on the regional breakdown of that?

Simon Tilford: There are statistics on the regional breakdown of that, yes. The proportion of immigrants coming to London who have a high level of education is much higher than the proportion going into Yorkshire. Having large numbers of skilled, highly productive workers boosts UK productivity, and hence growth and hence tax revenues.

John Mann: The regional statistics would be very useful to us.

Chair: Yes, could we have whatever you can reasonably provide?

Simon Tilford: Yes. There are clearly big differences on that.

Q27 Stephen Hammond: Good morning. I just want to ask a few questions about the potential impact of Brexit on financial services. We all know that in the 1990s, with the attempt to establish a single market in financial services, the passporting regime was established. How significant do you think that has been for British financial services over the last 15 years?

Roger Bootle: As with all these things, it is extremely difficult to tell. If we, as it were, reverse the question and ask what it would be like for the British financial services industry if we were outside the EU without our financial passport, what is so difficult to pin down is the extent to which this would really oblige firms operating in the UK and wanting to do business with the rest of the EU to operate an expensive branch presence and network on the continent. It would effectively mean perhaps that there would not be the same logic in operating on the same scale in Britain as well, and would therefore sharply diminish our industry—or can this effectively be overcome by the equivalent of a brass plate?

We know that the financial services industry's activities are highly fungible. All sorts of things move between one centre and another, and apparently they take place legally in one jurisdiction and have effect in another. It is very difficult to tell to what extent, if we were outside the EU, our financial services industry would be really seriously hit by the absence of passporting rights.

One thing is particularly significant. This has been a key issue with regard to Switzerland. However, the Swiss financial services industry has grown faster than the British during the period of our membership of the EU. I suspect that it is not a very heavy cost, but it is one of those things we simply do not know. Equally, it goes beyond passporting rights. There is a scenario in which you can imagine that, if the remaining EU wished to cause problems for Britain's financial services industry, they could act in a series of ways that would make it very difficult for our financial services firms.

Q28 Stephen Hammond: Thank you for that answer, because it brings me neatly on to a number of the more detailed points I wanted to ask. I take your point about the potential to establish a brass plate regime, but no one seriously thinks that that brass plate regime would be better than the current passporting system and/or, if we left the EU, the passporting system could be retained.

Roger Bootle: It is possible it could be maintained. That is something that would be up for negotiation. There would be several things to be negotiated if Britain were to leave, and that is one of them.

Philippe Legrain: It is extremely implausible. In Switzerland, which has the closest links outside the single market, banks need to operate often with subsidiaries in London in order to access the EU single market. Given the size of the UK financial services, and given the hostility that exists towards financial services and the so-called Anglo-Saxon model in other countries, it is extremely implausible.

Simon Tilford: I agree with Philippe on that. Were there a chance to achieve that, it would be only if Britain agreed to abide by all EU rules and regulations in this area despite having no say over them. That is the only way that we would manage to agree a continuation of the passporting regime.

Q29 Stephen Hammond: I would like to come back to that point in a moment. Just to go back to another point in Mr Bootle's first answer, you hinted that, notwithstanding the situation if we could not retain the passport regime and Goldman Sachs and JP Morgan were to say that is a key factor in influencing their decision to be in London, it would not necessarily mean a wholesale relocation of the headquarters of these investment banks because, presumably, you would argue the pool of talent, the agglomeration of support services in London and perhaps the time zone are equally key to the decision about where to locate.

Roger Bootle: Absolutely. One has heard these arguments several times before, notably in relation to Britain not joining the euro. A large number of supposedly very highly qualified people argued that there would be a mass exodus of the financial services industry if Britain were not in the euro. It did not happen. In fact, the reverse happened: it was the provincial continental financial centres that suffered, as business concentrated on London and, to a lesser extent, on Frankfurt. If anyone has any knowledge of the financial sectors in Frankfurt and Paris, it is perfectly obvious that they cannot hold a candle to what is on offer in London. Yes, if the financial services industry does not have passporting rights, there are going to be all sorts of difficulties and extra expenses involved in doing your business in London and having to operate some sort of branch presence or whatever it might be on the continent, but that does not necessarily mean to say that firms will up sticks from London altogether. Frankly, I do not think they can afford to.

Q30 Stephen Hammond: Can we pick up the implication from Mr Tilford's last remark? The Government have recently had to fight a number of actions by EU institutions that would have been perceived as damaging UK interests, including the proposal to force clearing houses to settle euro-denominated trades in a location other than London. Is it your view that there has been a determined effort by Brussels to curb the domination of the City?

Simon Tilford: No, I think that is rather fanciful. I know that many people in the UK see it in those terms, but they underestimate the influence that Britain has when it comes to financial regulation at EU level. There is no doubt that that influence has been eroded somewhat by the financial crisis and the at times rather self-serving tendency to blame Anglo-Saxons for the financial crisis, but Britain is still hugely influential in this field at EU level. Not everything that happens at EU level is detrimental to the financial services industry and Britain's financial services industry in particular, and it should also be recognised that, when it comes to re-regulating, if you like, the financial sector, Britain has been in the vanguard in a whole host of areas. The British have gone quite a lot further than many other Europeans have in this area.

There have been some foolish initiatives. I do not think it makes sense to control bonuses. If you control bonuses, the remuneration just comes out somewhere else. I am not saying that everything that happens at EU level has been sound but, as a whole, the idea that the rest of the EU is out to hijack the City just does not bear much scrutiny. There is no evidence for that.

Philippe Legrain: I do not think they are out to hijack the City, but there is clearly hostility to the City, not just elsewhere in the EU but also, indeed, among British citizens. That is actually a reason for staying in. If you think that Britain will be affected by EU regulation in financial services if it leaves the EU but it will have no possibility to build alliances to block harmful regulations, then that is a very good reason for staying in.

Q31 Stephen Hammond: The Governor, you will have noted, in a recent speech said that "actions to complete European monetary union should be taken with regard to their impact on all members of the European Union". Given your last answer, if we are either outside the EU itself or outside the Eurozone, are you optimistic that we will have an ability to control financial regulation, or do you see that there is a real chance of it just being enacted at the disadvantage of the UK?

Philippe Legrain: First of all, some financial regulation is broadly settled at global level, in the case of Basel III, which is what CRD IV basically transposes, and indeed in other areas. It is why it is good to have Mark Carney at the FSB. Is it possible that some EU financial regulations are going to overstep the mark and are going to be harmful for the UK financial sector? Yes, of course it is. Is that a reason to leave? No. Insofar as the UK is still going to be trading with the EU, and therefore still going to have to abide by those regulations, it is better to be in and have some say in shaping those regulations than to be out and to have no say at all.

Q32 Stephen Hammond: Would anyone like to comment on what they think are the prospects for Jonathan Hill's review of regulation post the crash and the CMU?

Chair: In a nutshell, or in writing.

Stephen Hammond: Or in writing, because it is quite a big question. I think this goes to the nub of our ability.

Chair: It is too big to answer so briefly, unless you have a well-formed thought on it. If that is alright, shall we move on and ask for something in writing? Do you have something you want to say orally, quickly?

Simon Tilford: Capital markets union clearly, in the long term, could be hugely beneficial if it opens up different sources of financing for companies across the EU. At the moment, financing is highly segmented. There could be very real benefits from that. The real benefits of capital markets union, though, come for the Eurozone, because the currency union needs to be able to spread risk. Unless you have highly integrated capital markets, that risk cannot be effectively spread. One of the reasons why the Eurozone crisis has been so deep is that losses incurred in one part of the currency union were not shared by private sector actors across the currency union as a whole. Whereas in the US, when Floridian banks and construction companies went bust, the losses were shared by people in Maine, in the Eurozone, when the same thing happened in Spain, the losses were concentrated in Spain and bankrupted the country's banks and then the state.

Capital markets union is crucial for the functioning of the Eurozone and, because of our obvious comparative advantage in financial services and all kinds of associated business services, we are best placed to profit disproportionately from the emergence of said markets. It is a long-term project. There is an awful lot of scepticism and opposition in various other member states. Clearly there is some political weight behind it at the moment, because politicians realise they need to do something, but the benefits from it will be a long-term thing.

Q33 Mr Jacob Rees-Mogg: If we are asking for written answers, we have not mentioned the financial transaction tax and the risk of the UK becoming the collector of that even if it does not apply it, which seems to be a major risk for the City.

I must not diverge from the questions I am coming back to on tariffs. There used to be very high tariffs. Those have come down, though the highest is still 56% for dairy products. Do we think from that that the EU diverts more trade than it creates? Perhaps, Professor Myddelton, you would answer.

Professor Myddelton: My answer is the same to all these questions, namely that I do not know. I should say, perhaps, I am not an economist; I am an accountant, so I am breathless with the expertise that my colleagues here have, but "I do not know" is going to be my answer most of the time, I think.

Mr Jacob Rees-Mogg: I am going to struggle on, because you are a professor and I know that professors know lots of things that will be useful to us.

Professor Myddelton: Of accounting.

Q34 Mr Jacob Rees-Mogg: I have a proper respect for professorship. Moving on, the tariff has come down from a 7.4% average in 1995 to 2.4% now, and the EU has concluded free trade agreements with countries including Mexico, South Korea and Canada. Do we think from that—and this perhaps you can answer,r because it is impressionistic rather than necessarily statistically provable—that the balance is moving in favour of trade creation away from perhaps a more “Fortress Europe”?

Professor Myddelton: Yes, but I deduce that from the fact that tariffs have come down. That is the key point. The closer you can get to free trade, the better.

Q35 Mr Jacob Rees-Mogg: The EU is making free trade agreements—30 of them so far—representing 23% of UK exports, and a further 70, representing another 42%, are under negotiation. Perhaps I ought to broaden this out to the panel: do we think that the EU is now becoming more committed to free trade and that these will reflect the UK’s interests in free trade?

Simon Tilford: Could I come back on the earlier question about trade creation and diversion? It is pretty clear that trade and investment between Britain and the EU are much higher than can be explained by economic size or geographic proximity, and there is very little evidence of trade diversion outside of agriculture. In agriculture, clearly, there has been some trade diversion, but agriculture accounts for a very small proportion of trade. There is very little evidence that EU membership has impaired British exports to non-EU markets, but there is an awful lot of evidence that trade and investment are much greater than they otherwise would be. The big question is what would happen to that much higher level of trade and investment were Britain to leave. That depends on the kind of deal Britain puts in place with the EU on leaving.

Q36 Mr Jacob Rees-Mogg: Would you like to come on to the next question about whether our interests are being reflected in these trade deals? Perhaps, Mr Bootle, you might like to give your view.

Roger Bootle: Yes, I have a couple of points. First of all, the evidence seems to suggest that the EU has not been very good at negotiating trade deals. It is very slow and cumbersome. There is an interesting argument about this. Various people say that Britain would surely be better placed being part of a big bloc with clout in negotiating trade deals than being on its own, the small island that we are. There is that possibility, but there is also another possibility, which is to say that if you were part of a larger bloc, in fact, it might be quite difficult to get your interests effectively represented by that bloc and you would end up with a worse trade deal than if you negotiated one separately. It is very difficult to be sure of the answer to that, but we do know that lots of small countries around the world have successfully negotiated free trade deals, including with very large countries like China.

Q37 Mr Jacob Rees-Mogg: Historically, the UK has been more open to free trade than other EU countries, and some of the deals get delayed by relatively obscure interests—parmesan cheese and French films—clouding deals that we are trying to work for.

Roger Bootle: That is true. One has to take account of the fact that the structure of our economy is very different from the structure of most continental European economies. We have a much bigger financial services sector. We have a much smaller agricultural sector than is true of France, a much bigger business services sector than is true of most of those countries, and smaller manufacturing than Germany. It is by no means obvious that getting your negotiations for the interests that really affect you done by this bloc of which you are a member is going to be more effective than doing it yourself.

Q38 Mr Jacob Rees-Mogg: Would you like to put the counter-argument?

Philippe Legrain: First of all, on your first point, it is clear that because deepening of Britain's economic relationship with the rest of the EU has gone hand in hand with tariff liberalisation it mostly is trade creation, although I would agree with Simon that there is clearly trade diversion in the agricultural sector.

In terms of negotiating trade deals, bilateralism and preferential trade agreements are second best to WTO deals, so I would be sceptical about the merits of these bilateral deals, whether they are conducted by the EU or by the UK. What is clear, though—I was previously special adviser to the head of the World Trade Organization—is that size matters. Yes, it is true that small countries can negotiate trade deals with the United States, but they are one-sided. The USTR comes in with a set of demands and it is "take it or leave it", and then you take your chances with Congress ratifying. The idea that Britain is going to be able to negotiate a better trade deal with the US than it can as part of the EU I find fanciful. We saw an example of that when Britain negotiated an extradition deal with the US bilaterally under the previous Labour Government. It was completely one-sided. It gave rights to the US that were not allocated to the UK. Yes, you are right, Roger, that in some cases obstacles such as French protectionism can hold up the negotiation of the TTIP agreement, but overall, negotiating as a big group you are going to get a better deal than you can on your own.

Q39 Mr Jacob Rees-Mogg: Professor Myddelton, I come back to your classic protectionist argument. If you believe in free trade, the abolition of all tariff barriers is to your advantage, regardless of what other countries do in response.

Professor Myddelton: Yes. The essential point is that we are different from them, as General de Gaulle said 50 years ago. We are different.

Philippe Legrain: With all due respect, that is not a protectionist argument.

Q40 Mr Jacob Rees-Mogg: Hold on. I was asking Professor Myddelton. We want to get some balance in the talking from the members of the panel. You bring down consumer prices; you allocate resources better. If you believe in free trade, one-way free trade agreements are not a problem for the person who is the most open; they are a problem for the person who is the more closed.

Professor Myddelton: I agree with that.

Philippe Legrain: With all due respect, that is not a protectionist argument at all. I am a free trader. I have written several books on this. It is really not true, because modern trade agreements are not just about liberalising tariffs. They are also, for example, about things like protecting intellectual property, which restricts trade. If the US comes into the UK and says, "We want all sorts of intellectual property restrictions", which are in effect extracting rent from the UK economy by US companies, then, if you are negotiating a one-sided deal, it is actively detrimental to the UK. It is different from simply liberalising tariffs, in which case you are absolutely right that you should unilaterally embrace free trade, whatever the rest of the world does.

Q41 Mr Jacob Rees-Mogg: Excellent. Thank you. You would have free trade regardless of what the rest of the world does, fundamentally. That would be your point.

Philippe Legrain: Absolutely.

Q42 Mr Jacob Rees-Mogg: But the EU has not so far provided that for us. To some extent, the common external tariff has hindered UK trade.

Philippe Legrain: The UK tariffs have fallen since joining the EU, and we do not know what would have happened had we not joined the EU. Clearly, there has been a global trend of falling tariffs in manufacturing, but one does not know the counterfactual.

Q43 Mr Jacob Rees-Mogg: Mr Bootle, do you have a thought on this?

Roger Bootle: The key factors here are the falling tariff rates in general and the falling relevance of goods trade as opposed to trade in services, particularly for this country. We are not going to settle these various issues, I do not think, about trade diversion versus trade creation. There are lots of studies on this issue dating back to since we first joined what we then thought of as the Common Market, but the trends are very important. However important it was to be in the EU in order to get inside the tariff barrier in 1973, the evidence is it is much less important now. The tariffs for everybody are much lower. That is part of a general world trend. It is not just about the EU; it is happening across the whole world. Our manufactures, as a part of our economy, which is the only bit that is subject to tariffs, let us face it—it is a very important point that services are not subject to tariffs—are a smaller share of our economy than they were in 1973. The relevance of this argument has been greatly diminished over the years.

Simon Tilford: The relevance of the tariffs argument might have diminished but, as Roger alludes to, a rising share of our exports are accounted for by professional services, business services and other high value added services. Obstacles to the trade in those services are not tariff-based; they are non-tariff-based. Breaking down those obstacles is a very difficult and protracted affair. It is the area in which the EU has done much work, but there is much left to be done. The WTO, for example, has made virtually no progress whatsoever in breaking down barriers to the trade in services, so we will be pulling out of a single market that has done quite a bit and will do more in the future in an area where we have a huge comparative advantage and that accounts for a rising proportion of our overall exports.

Q44 Mr Jacob Rees-Mogg: Though we may be able to do it for ourselves.

Simon Tilford: We may, but only by signing up to all the rules and regulations, which would obviate the case for leaving, I assume.

Q45 Mr Jacob Rees-Mogg: Not with the rest of the world. With the rest of the world, we could make the agreements that we wanted and would be free of overarching European regulations.

Simon Tilford: Again, that comes back to the points that Philippe was made. Would, for example, Britain have more success in prising open Indian markets for commercial services if we were doing it on our own than as part of the EU as a whole? I tend to agree with Philippe on this one; I do not think Britain would be that effective on its own.

Philippe Legrain: The word “free” is kind of misleading, because any trade agreement involves a constraint on sovereignty. That is true of a WTO agreement; it is true of a bilateral trade agreement or an investment treaty. You are constraining your Parliament’s ability to act because you think that it provides an economic benefit.

Q46 Mr Jacob Rees-Mogg: No, because you do not have a court that is automatically the law in your own country. The sovereignty issue is not really relevant to the trade negotiations.

Philippe Legrain: Yes, it is.

Simon Tilford: It is.

Q47 Mr Jacob Rees-Mogg: Not unless you have a sovereign court that can overrule you, because you can pull out of trade negotiations with other countries. This is not immediately relevant.

Just one final question, and a technical point really. There are the existing trade agreements that we are signed up to. They are joint competence between the EU and the UK. I do not know if any of you know or wish to express a view as to whether we would be able to continue in those as they are because they are joint competence, or whether they would all need to be renegotiated from scratch.

Simon Tilford: As far as I am aware, they would all need to be negotiated from scratch.

Q48 George Kerevan: I was going to pick up on the point that Jacob has just raised, because I think it is key. I would like to get the view particularly of Mr Legrain given his experience with the President of the Commission. The issue is: if we leave, do we have to renegotiate all of the existing free trade or trade agreements between the EU and the rest of the world as an individual country?

Philippe Legrain: Yes.

Q49 George Kerevan: How long do you think that might take?

Philippe Legrain: It could take a long time. Bilateral trade deals take a long time to negotiate generally.

Q50 George Kerevan: What happens to UK trade relations with other countries in the interim?

Philippe Legrain: They would be governed by WTO rules if there is no trade agreement between those two countries. Clearly, in some areas—in many services—there are no WTO rules. If the FTA included services provisions and we were no longer party to that FTA then, in the case of services, we would have no right of access to that market at all.

Q51 George Kerevan: Would that impact, Mr Bootle, particularly on the City of London?

Roger Bootle: It might well do. Let me just say that I am not sure I agree with this notion that all these agreements are bound to be renegotiated from scratch. I think it is worth the Committee investigating this. I will try to do some establishment of the facts. I think this is a legal issue. My understanding was that in some cases they would need to be negotiated from scratch and in some cases they would not. It is an important question and I think we should try to nobble it.

Q52 George Kerevan: It is more than important. It goes to the heart of the future of the City. Do we know if the City has done any kind of background analysis of this? No? I think that will be part of our investigations on this.

To take that issue a little bit further, we are in the middle of EU-US negotiations over a new trade agreement, and I noticed that Iain Mansfield, in his very interesting essay on how Brexit would play out, suggested that the alternative would be for the UK just to negotiate a side deal with the United States. I wonder if any of the panel, given their experience, would care to comment on how easy or difficult that is or how long that might take.

Simon Tilford: I do not think it would be a big priority for the Americans, for the reasons we have already discussed. Britain is already hugely open, so we do not have much to give and trade deals are increasingly about reciprocity. You give something; I give you something in return. This is one reason why we benefit from negotiating these deals from within the EU, because we benefit from the protectionism of other EU countries. The EU has something to bargain with. It has some leverage. The British economy is already incredibly open to the Americans in the sectors that they want access to. They are also determined that we do not leave the EU, so I do not think they will be falling over themselves to negotiate such a trade deal and, anyway, it would not help address the loss of access to the single market were we to leave.

Q53 George Kerevan: The Americans are interested in accessing, let us say, some of our service markets, such as health.

Simon Tilford: Yes, in that sector, but, again, is there a majority in the UK in favour of allowing that to happen? I do not see any readiness in the UK to open up healthcare to international competition.

Q54 George Kerevan: Which leads to the conclusion that a Brexit is most likely not to lead to the UK being able to negotiate a further enhanced trade agreement with the United States, if we are not willing to offer our end on health.

Simon Tilford: I suppose it could. I do not know if such a negotiation would falter on the issue of healthcare. I am afraid that is outside of my area of competence. I am sorry.

Q55 George Kerevan: Understood. It is just that much has been made in the UK, both within the business community and within Government, of the need for TTIP. That is why I am interested in probing that. If leaving the UK paradoxically makes it more difficult to negotiate with the Americans, then that would be an issue both for Government and for others.

Philippe Legrain: It depends on how much of a political priority it would be for the British Government after we left the EU. One can envisage circumstances whereby the Government would want to make it a priority, in order to show that Britain could trade more with the US outside the EU. Then, if that was a matter of urgency, one could imagine the Government making all sorts of concessions in order to clinch that deal, but that is a hypothetical.

Q56 George Kerevan: The free trade issue also takes us into the relationship with China. As we saw last week, China is clearly anxious to develop its Silk Road project with Europe. Again, I know we are in hypothetical grounds, but particularly for Mr Bootle with his knowledge of the City, is a UK exit from the EU going to make it easier or more difficult, do you think, to negotiate trading relationships with China?

Simon Tilford: Again, I suspect it would make it much harder. If one looks at the Swiss bilateral trade deal with China, the Swiss did not get much from that. They opened up across the board to China, which I agree is in their interest, but only extracted a promise from the Chinese to do various things at future points in time. Britain is a much bigger economy than Switzerland and I suspect it would have slightly stronger cards. Having said that, I refer to my previous point, which is that this is already an extremely open economy, so it does not have that much leverage. When it comes to accessing the Chinese market, that is a prima facie case of where acting within the EU is a positive for the UK. I cannot see a bilateral deal delivering the kind of market access to China that an EU deal would do.

Roger Bootle: It is very difficult to say how easy it would be to negotiate. I have already laid out the principles here. You would have more clout in the sense of being part of a bigger entity that has more market muscle, but that does not end the issue because, in being part of a bigger entity, you also have to compromise with other members of that entity. It is by no means obvious that, simply because you are a bigger outfit, you end up with a better deal. There is quite a lot of evidence on this. A lot of studies have been done.

You will notice that all these countries that do not benefit from being in the EU or indeed some other larger bloc have done extremely badly and are very poor: Switzerland, Singapore—we can go on and on and on. I am afraid this notion that just being part of a large bloc gives you an automatic passport to prosperity really is economic nonsense.

George Kerevan: I would not say that Switzerland or Singapore were poor.

Roger Bootle: The point that was made earlier about the benefits of free trade is a critical one. Simon is right that if you open up your markets completely without some sort of quid pro quo from another country you do not have anything to give, as it were, and therefore you are in a weaker position to force them to open up. Throughout this debate—I do not mean in this room, but in general—the presumption is that the benefits of trade come from exports only. They do not. They come from exports and imports. The notion that we would, in some sense or another, be in a terrible position in opening up our trade without being able to force them to open up their trade I am afraid is economically illiterate.

Philippe Legrain: It is right that opening up to imports provides a big economic benefit. I would be in favour of unilateral free trade, whatever relationship we are in with the EU. The reality is that exports also provide a benefit, because they enable us to pay for imports, and therefore we also want to try to negotiate as good access to foreign markets as we can. Thirdly, most trade negotiations now are not about market access; they are about rules, regulations, protection for intellectual property and all sorts of associated issues. Where clout matters, because basically it is about the allocation of rents, the one that has the most clout is going to grab the rents.

Q57 George Kerevan: I agree with that analysis. On the China issue, it seems to me that China's Silk Road strategy is aimed at creating a preferential relationship with the EU as an institution and as a political bloc. I am just curious to get your opinion. If the UK were to leave that bloc, would that not surely leave the UK outside the Chinese perspective of what it wants to achieve?

Philippe Legrain: President Xi said very clearly, and it was repeated by the ministry, that China wanted Britain to remain within the EU, because, while they want to develop economic relations with the UK, they think they are best served by keeping Britain in the EU. I do not think they are alternatives. There is this false debate that goes on that sets up EU relations versus global, and they are not; they are complementary.

Chair: I am sorry that we have nothing like enough time with each of these questions to develop in more detail some very interesting subjects. Part of the problem is we have Treasury questions on the Floor of the House immediately following this session, and so we need to finish at 11.15 promptly.

Q58 Mr Steve Baker: Are we all agreed that unilateral free trade is a good thing? I think Mr Legrain has just said he is in favour of unilateral free trade. Is anyone not in favour of unilateral free trade? You do need to speak otherwise it is not on the record. Nodding is not enough.

Professor Myddelton: Yes, I agree.

Simon Tilford: Yes, but you also need to work hard to ensure maximum access to export sectors.

Mr Steve Baker: I will come on to that in a moment. Mr Bootle, unilateral free trade?

Roger Bootle: I do not like signing up to any open statement like that. There are circumstances in which I would not be in favour of it, but my presumption would be, yes, that it is a good thing.

Q59 Mr Steve Baker: To what extent in the contemporary world do we need to sacrifice sovereignty in order to achieve free trade or free trade agreements, such as they are? Is it possible to have unilateral free trade in a sovereign nation, in the world as it is?

Philippe Legrain: One can open one's markets unilaterally without needing to sign any agreement with anyone. In order to gain access to, or for your firms to be able to operate in, other markets, you do need to negotiate under the presumption that other countries either do not maintain unilateral free trade or regulate their economies in some way. I think those assumptions hold.

Q60 Mr Steve Baker: I would like to tease some of this out with Professor Myddelton in particular. I do not wish to pick on you, Professor Myddelton; I wish to be helpful, but I would just like to tease out a couple of things. Earlier on, you said that your answer to most questions would be "I do not know". I did not take that to mean that you wished to come here and waste a seat on the panel; what I really understood you to be saying was that the answer to most of these questions is unknowable, rather than that you personally do not know. Is that right?

Professor Myddelton: Both, yes.

Q61 Mr Steve Baker: I am trying to get some helpful evidence from you, Professor Myddelton, but the reason you do not know is often because it is unknowable.

Professor Myddelton: Yes. We are talking about the future, remember, which is by definition uncertain. There is a lot of uncertainty even about the past. To begin with, we were flashing around economic statistics that are just nonsense. They are just propaganda and we got that conclusion from all of us, pretty much.

Q62 Mr Steve Baker: You are hinting at what I think we would describe as the epistemological problem in the social sciences: that most of the information that is needed is just not available.

Professor Myddelton: Yes.

Q63 Mr Steve Baker: The other thing that came out in your evidence was that you seem to be quite despairing of the prospects for enlarging liberty and free markets. Is that a fair characterisation?

Professor Myddelton: No, not really. There has been enormous progress towards liberty over the last 100 to 200 years, so we have not done so badly, but there are always political pressures against it. We have to keep the fight going. I am optimistic.

Q64 Mr Steve Baker: That is not quite what I understood from an earlier comment. I notice—I do not think he would mind me saying—that our colleague Kelvin Hopkins, who is a Labour Member of Parliament, criticises the European Union for being a neoliberal project. Would you think that it is a fair characterisation to say it is a neoliberal project?

Professor Myddelton: "Neoliberal" is not an expression I am very comfortable with but, no, his meaning is probably incorrect.

Q65 Mr Steve Baker: Do you think it is possible that the European Union has managed to simultaneously dissatisfy both advocates of free trade and liberty, and socialists?

Professor Myddelton: It is hard for me to speak for socialists. I think it has managed to dissatisfy an awful lot of people, yes.

Q66 Mr Steve Baker: I want to focus on regulation. Can I ask each of you what estimate you have made of the amount of regulation that comes from the European Union and is applied in the UK? How much of our regulation either comes from Europe or is influenced by it?

Professor Myddelton: I do not think we should downplay the ability of British regulators to smother the economy in red tape.

Q67 Mr Steve Baker: But what proportion would you say comes from the European Union?

Professor Myddelton: My usual answer there, I am afraid: I haven't a clue.

Roger Bootle: I am going to invoke the same defence, I am afraid: I do not know. To come up with any reasonable estimate of this is a pretty big enterprise. There are some studies on this. They tend to be heavily ideologically motivated on one side of the issue rather than the other, which is a problem, but there are a number of studies that the Committee can benefit from.

Q68 Mr Steve Baker: I am looking at a couple of studies here. The House of Commons Library has estimated that 7% of primary legislation and 14% of secondary legislation made in the UK had a role in implementing EU obligations, but Business for Britain went on to take into account EU regulations that are directly transposed into national law and came up with the answer that, between 1993 and 2014, 64.7% of UK law could be deemed to be EU-influenced. EU regulations accounted for 59.3% of all UK law. Do you think that they are right that the majority of UK law is now EU-driven?

Simon Tilford: I do not think they are, no. The more interesting point is how much of that regulation would be renationalised were we to leave the EU. This idea that all of this regulation at EU level would not apply and that we would not replace it with national regulation is inaccurate.

It is worth bearing in mind a couple of things when it comes to regulation and the EU. The EU does not enforce rigid harmonisation of regulation across the EU. If we look at, say, labour market regulation, according to the OECD, which I trust people are confident in, we have similar levels of labour market regulation to the other English-speaking countries and far lower levels than the rest of the EU. When it comes to regulation of services markets and product markets, we have the least regulated product and services markets in the world, after the Netherlands, another EU country. The idea that the EU is some kind of regulatory straitjacket really does not pass muster.

Also, something that has iconic status in the UK when it comes to EU regulations, the working time directive, is a stupid piece of regulation but, if it were having a huge impact in the UK, there would be a spike in the number of people working 47 hours 59 minutes a week. There is no spike. There is a little spike, but there are big spikes at 40 hours and 50 hours. I am not saying it is a sensible piece of regulation. I would like it to be overturned. On the regulatory stuff, lots of things would be renationalised. We are still a very liberal, open economy, despite EU membership. It does not command us to regulate our economy like the French. Some of the things that exercise people most have less impact than is commonly understood.

Q69 Mr Steve Baker: You have mentioned three things there that I would like to pick up. What is your evidence for dismissing the figure that Business for Britain came up with? It seems quite a detailed study to me.

Simon Tilford: I would have to look at it very carefully. They have a very strong agenda, so I would have to look at the assumptions they have made and how they have come up with that figure. I do not know; I am not familiar with the piece of work. It contrasts very sharply with pieces of work put together by other people, but some of those other people have an agenda too. One has to look at the politics of the organisation in question and then carefully look through the assumptions they have made. As for that piece of work, I do not know.

Q70 Mr Steve Baker: I want to bring in Roger Bootle, but I am conscious that we seem to be coming back to this issue of "I don't know".

Chair: Excuse me, Steve. Just before we leave that subject, if you have time to take a look at those assumptions and drop us a line, we would be extremely interested. I noticed that throughout that exchange, Professor Myddelton has been nodding his head or certainly responding vigorously in various ways facially, and still is. I would be grateful for your views on it too, if you get the chance.

Roger Bootle: Surely this question of to what extent, if we left the EU, we would replicate EU regulations in this country depends critically upon one's assumption about the political regime in this country. What regulations would be abandoned or adopted as UK national legislation would be greatly affected, surely, by whether we had Mr Jeremy Corbyn as Prime Minister, for instance. We cannot come up with an objective view as to what the situation is going to be. It depends on what the UK chooses.

Mr Steve Baker: We are back to imponderables and "we do not know".

Philippe Legrain: That is true, but if you look at the costliest regulations as identified by Open Europe, they identify the most expensive as renewable energy. The fourth is the EU climate and energy package. There are climate negotiations ongoing and potentially a deal in Paris, and the UK presumably, even outside the EU, would be party to those negotiations and most likely we would have equivalent regulations. I have already mentioned the second most costly, which is CRD IV, which transposes largely Basel III, which most likely we would also be party to.

I agree with Simon on the working time directive, which is the third most expensive. I would go further and say that the common agricultural policy is probably the worst thing about the EU, except that, even before Britain joined, we had support for farmers and it is pretty likely we would have support for farmers afterwards, first of all because of the lobbying power of rural landowners, and second of all because of eco-romantic localists who want to have food production here in Britain, plus associated concerns about food safety and blah, blah, blah. I think it is actually quite plausible to say that there would be equivalent regulation—in some cases less, perhaps, but in some cases also more.

Q71 Mr Steve Baker: Mr Tilford gave me a rich seam because, as he was talking, I was reminded that I read that the Trans-Pacific Partnership requires that participants abide by United Nations International Labour Organization rules. Is it not the case that, increasingly, the international regulation that is required is global rather than European? Is it not the case that, if we were not in the EU, we would have direct influence over the global bodies setting rules rather than allowing ourselves to be represented by the European Union?

Philippe Legrain: In the trade agreements that the US now negotiates, they insert clauses to protect labour standards, which are in effect protectionist to help US workers. Most likely, insofar as there were ways in which US unions thought that there was unfair competition from British workers, those could be imposed on us as part of a US-UK hypothetical FTA. Otherwise, there are not global labour standards enforced by the ILO.

Q72 Mr Steve Baker: That is one of the key points: that it is not subject to the ECJ. Does anybody else wish to add to that? Otherwise I have one last question. Nick Clegg said, "Let's make sure that small firms which don't export, such as hairdressers and newsagents, are exempt from EU regulation unless there's a cast-iron reason". It has been estimated that less than 6% of businesses export goods abroad, but 100% must comply with EU law. Is it fair and efficient that everybody has to face this regulatory burden, when so few as a proportion export?

Roger Bootle: I am not sure whether "Is it fair?" is the right question to ask. Is it efficient? Is it beneficial? I can probably talk to that. No, I do not think it is beneficial or efficient. It is perfectly understandable from the point of view of the EU authorities. I am interested in how Nick Clegg thinks that this objective would be achieved of exempting the rest of the economy that does not export. The reason why it is understandable is that what the EU is about is trying to create a level playing field, if you like—a sense of commonality—across the whole of the EU whatever activity you are in. The working time directive applies whether you are in the exporting business, hairdressing or whatever. That is understandable.

From the point of view of the costs to Britain of leaving the EU, it is a vital part of the argument that large parts of the economy that have nothing whatever to do with exporting are nevertheless subject to EU regulations, to come back to where we were just a moment ago, and therefore it would be possible to relax the burden of regulations on those businesses without any adverse effect on export performance. Whether we would relax the regulatory burden is precisely what we were talking about a moment ago.

Q73 Mark Garnier: To carry on from that on this whole business of regulation, surely there are a huge number of regulations that are coming through from Europe that we would have implemented ourselves anyway, in terms of working standards, making sure people do not fall off ladders and that kind of stuff. Although sometimes we think they are rather ludicrous, is it not the case that the vast majority of this stuff we would have done as a civilised society anyway, and we have devolved the effort of having to write these rules to Europe?

Roger Bootle: That is the essence of the problem in estimating what sorts of sums should be attributed to the cost of regulation. If you look at the studies of those people on the side of the debate who favour withdrawing from the EU, first of all, they attribute a very large cost to regulation—that is a very murky area as well—and secondly, they assume that outside the EU we would not have enacted these bits of regulation. We really are, I am afraid, in the realm of the completely imponderable. What we do know is that if we were outside we would be able to choose our own set of regulations. In principle, we would be able to set regulations at what we thought was the appropriate level and type in regard to their cost and their applicability to the UK economy. Quite where that pans out, as I said earlier, is impossible to tell. Surely it would switch with the changes in the political climate and who was governing the country. There is not a single answer for both Labour and Conservative Governments.

Q74 Mark Garnier: Absolutely. What I really wanted to talk about was foreign direct investment. I will come back to you, but perhaps I can start with Philippe Legrain. Ernst & Young did a 2015 UK attractiveness survey and came up with some very interesting numbers about foreign direct investment coming into the UK. The numbers speak for themselves: a record number of 887 projects, up 11% on 2013—this is for 2014—and increased European market share, with a market-leading 31,198 jobs created. Just how important is being a member of the EU to attracting foreign direct investment into this country?

Philippe Legrain: It depends on the sector. In the case of financial services, which is roughly half of FDI to this country, we have already discussed the fact that access to the EU single market is an important reason why foreign firms invest in the City of London and other financial centres in Britain. The same is true for the foreign-owned car industry, which mostly exports, and a large share of that to Europe. In other sectors, it will be more specific to Britain. In any case, firms invest for a variety of reasons, partly due to the particular qualities that Britain has, whether it is a skilled labour force or whether it is the domestic market, and partly due to the fact that it has access to a single market of 550 million people.

Q75 Mark Garnier: When you start breaking down how we perform in terms of FDI into the UK compared to the rest of Europe, it seems that the UK grew its software and financial services sector projects, capturing 35% of all European headquarter moves, and led Europe on research and development projects. We have 29% of US projects in Europe, and are the main destination for investment in Europe from France, Japan, Australia, Canada, India and Ireland. The fact is that, when you are looking at FDI coming into Europe as a whole, we are a leading exponent of that. How would you explain that? It sounds like a very positive thing. On the one hand, you have people coming to Europe and, on the second point, if they are going to come to Europe, they tend to come to the UK. That is a pretty amazing advantage, is it not?

Philippe Legrain: Britain is a very attractive economy to invest in, whether it is because of the flexible labour market, the high level of skills, the rule of law, membership of the EU, general openness, political stability, the English language, the golf courses or all sorts of other things.

Q76 Mark Garnier: I appreciate all of that, but, as you know, this is a specific inquiry into the benefits or otherwise of being a member of the EU. Whilst we all like to think we are lovely, charming people here and have very nice arts, the question is to what extent you think this is to do with Europe. What would be the risk to the UK were we to come out of Europe? Would we still see people coming here because they like the weather and the culture, or would they be less inclined to come because the UK would no longer be a gateway to Europe?

Philippe Legrain: You cannot give a precise answer. I think that, overall, in some cases they would be less inclined to come, because we would not have the same access we have to the single market in financial services, or indeed because of the tariff that would be imposed on car exports. You cannot quantify how large that would be and there are lots of imponderables, as Roger is doubtless going to say.

Roger Bootle: Yes, there are imponderables about this, but I was going to say something else. It is possible that what happens to foreign direct investment is determined by factors other than everything else we have been talking about, but it is unlikely. It seems to me that, other than the immediate short term, where uncertainty might play a big role, whether foreign direct investment is greater or less than it has been recently into the UK after a Brexit would depend an awful lot on how successful it was. That is to say that, supposing we left and we were not able to negotiate a very favourable trade agreement with regard to manufacturers, the City, and so on and so forth; supposing also we did not rescind lots of regulations; supposing, in the worst-case scenario, we were still shoving our budget contributions towards Brussels; and supposing the job impact of the loss of trade with Europe was very severe, the overall economic performance of the UK would be pretty poor. In those circumstances, would we expect FDI to be the same, lower or higher than it was before? I do not think it is difficult to answer the question.

There is another possibility, which is that we leave the EU and none of these awful things actually transpires: we forge a pretty good trade agreement with the EU, including financial services; we do cull some regulations; we save our budget contribution; there are not any net job losses; industrial consumer confidence is quite high; it looks like the UK economy is actually pretty well placed; and we are negotiating free trade agreements all round the world. What then happens to FDI? The answer is that the UK becomes an even more attractive place.

Q77 Mark Garnier: I think that is a very important point. You wrote a note, *The Trouble with Europe*, and I refer to page 270. No doubt you will remember exactly what that is but, for everybody else in the room who perhaps has not read it, you talk about this whole thing about FDI and the benefits, but you also make the point that, were a Japanese car company to close down and we had come out of Europe, to say that is lost jobs and lost assets is a misunderstanding of what would happen. You talk about the fact that what would happen is that those workers would then become available for another industry, another type of business and all the rest of it, and those factories could be used. What do you suggest would be taking their place? Why would people necessarily be creating businesses in the UK when clearly the single market could be more attractive? I am not trying to lead the answer; I am just trying to get an idea of what your vision is.

Roger Bootle: This depends upon the overall attractions of the UK economy and its effective functioning. We heard earlier on about the lump of labour fallacy. There is no fixed number of jobs to go round. New jobs can be created effectively out of nowhere. It depends upon how the UK trades with the rest of the world. It depends upon the effectiveness of the economy domestically. If we did save our budget contributions, for instance, what would we do with that money? A whole series of factors like this would influence where new jobs appeared and where new industries prospered.

Q78 Mark Garnier: We have been talking about how difficult it is to try to understand what is going to happen, given certain things happening, and trying to war-game what would happen if you come out of Europe, if you stay in Europe and all the rest of it, but you have given quite a lot of thought to this. I am going to press you, if I may, just to really get an understanding of how you see the UK flourishing outside the EU. There are an awful lot of people who see the status quo as being safer and easier to understand. It is something we can get our heads around. We do not like a lot of regulation, but we understand all of that. If we are going to go out into the unknown, what people will be looking for in this debate is arguments from people like you. You have identified this particular point. From the point of view of this Committee, it would be really helpful if you could perhaps dive deeper into your vision of this and really talk more about types of businesses. When you are war-gaming on all this, you have to have a certain number of things that happen to come out to an end conclusion. On this particular one, you possibly have an awful lot of things. There are probably more things that need to happen for what you suggest to happen. I just want to see if I have got that completely wrong.

Roger Bootle: First of all, on your expression about diving out into the unknown, I do not think that is the right way of looking at things. Staying in an unreformed EU is also diving into the unknown. We do not know how this particular association of countries is going to develop and the current signs are not very favourable. That is to say it is an over-regulated and, I would argue, malfunctioning entity that is spreading its tentacles ever wider. The economic record speaks for itself. That is pretty much unknown. We cannot escape unknowns.

What sort of vision would there be for Britain? First of all, I would want Britain to try to secure a close trading agreement with the remaining EU. That is eminently achievable. It is not certain, but it is eminently achievable. I would not seek to remain part of the single market. I would not want the Norwegian arrangement, because along with that goes all the regulations. You cannot have it both ways. I would seek to stand outside that set of arrangements, but with a very close trading relationship, and seek to gain as many and as close trading relationships as possible with the rest of the world.

A key factor in my approach to these questions is the past trends and the likely future trends. As things stand, unless something fundamental alters, the EU is a fading economic entity. Its share of GDP is falling sharply. Therefore, the relevance of this question is diminishing too, compared with when we joined it. It is falling sharply for a number of different reasons. First of all, it is the rise of the emerging market powers around the world, led by China but not only China. That faster growth is inevitable. Secondly, it is a demographic feature of Europe. The demographics look pretty awful. Over and above that, it is also the failure of economic policy in Europe that has meant that European GDP per head has been growing slowly. More recently that is primarily because of the failures of the single currency. This is a very important factor: that the rest of the world is getting bigger relative to the EU. I would want Britain to make sure that it plugs into the rest of the world.

Q79 Chris Philp: I would like to concentrate on the question of the United Kingdom's contributions to the EU budget, which for the last financial year will be about £18 billion on a gross basis. I would like one of the panel members to comment on the way that figure has been publicly presented. Sometimes the gross figure is given with no account for the rebate or EU public spending in the UK. I wondered if you could comment on what your view is of the most honest way of presenting those budget figures. Maybe Simon Tilford or Professor Myddelton could comment on that.

Professor Myddelton: It is quite a small percentage of GDP. I do not get very excited about it. If that is all we are worried about for the EU, it is a tremendous non-problem.

Q80 Chris Philp: It is clearly one element of many. We got very excited last night about £4 billion and this is £18 billion. On the question of presentation, Mr Tilford, perhaps you could comment.

Simon Tilford: One needs to acknowledge the difference between gross and net, because the net figure is less than half the gross figure. If we want an informed debate about the scale of our contributions to the EU budget, we have to look at both. The net figure is relevant. Of course, like all of the data regarding this issue, it is used selectively by the two sides to score political points.

Roger Bootle: It is probably right to look at both the gross and the net, but if you had to choose only one to focus on, it would surely be the net, which would represent the net loss of financial resources from the UK overall. I think I am right in saying that comes out at about £11 billion. I was struck by the fact that in recent documents from the Vote Leave campaign I saw the other day—and I should declare an interest, because I am associated with it—they were talking about £11 billion as being the cost of our contribution.

The reason why it is sometimes right to look at the gross figure is that some of these amounts that you are paid back you are getting back financially, but you may be getting them back in ways that are very damaging or at least you are not getting full value for them. That is to say that they might amount to subsidies for a whole series of things and, if you had the money to use yourself, you would use the money better. I would focus on the £11 billion, the net figure, but I would not altogether disregard the gross figure.

Philippe Legrain: The net contribution is actually £8.4 billion, which amounts to £130 per person per year, or about 35p a day, which is less than a pint of milk per person, per day.

Q81 Chris Philp: You are clearly in the camp, Mr Legrain, that thinks it is a relatively small amount of money.

Philippe Legrain: It would be better not to make a net contribution at all but, given the way the EU is financed, that would require us to become poorer, and I would rather we be richer and be paying to be part of the club than be poorer and not be paying to be part of the club.

Simon Tilford: The bigger issue than the amount of money is how it is spent.

Q82 Chris Philp: That brings me on to my next point. I am glad you raised that. The EU budget, I think I am correct in saying, has not been signed off by the auditors for something like 25 years. The Chairman will correct me. It is some length of time of that order. Can you comment on the appropriateness of the United Kingdom taxpayer, who is currently quite hard-pressed, as we have been hearing recently, contributing to a budget whose own auditors would not sign it off? If this was a company, the board would have been sacked years ago.

Professor Myddelton: That is a somewhat misleading comparison. The fact is, there are technical reasons why the auditors feel unable to sign off the accounts, as you say. What I find even more absurd is that the accounts go to the nearest cent, I believe, in Europe, not even the nearest euro. They are presented to a ridiculous degree of accuracy, which is completely misleading, but I would not worry too much about the auditors. I really would not.

Q83 Chris Philp: Can you elaborate on that a little? You say there are technical reasons. Can you give us a flavour of what those technical reasons are and why we should be unconcerned that the auditors do not sign off the accounts?

Professor Myddelton: Tracing some of the expenditure is extremely difficult, and that is generally recognised. That is why the auditors are reluctant to sign the accounts.

Q84 Chris Philp: In terms of the unaccounted-for expenditure, can you give us any feel for the magnitude? Clearly, if it is 0.5% of the budget, one might take a view that that is de minimis, but if it is some significant portion of the budget, it would be more concerning.

Professor Myddelton: It is much more significant than that. It is quite significant.

Q85 Chris Philp: Can you give us a feel for quantum as a percentage?

Professor Myddelton: 5%. I am guessing, really.

Q86 Chris Philp: That is the percentage of the total that is unaccounted for as disappeared in some way.

Professor Myddelton: Yes.

Q87 Chris Philp: I think I am right in saying that that is not the case with United Kingdom Government expenditure.

Professor Myddelton: I will not comment on that, but I do not necessarily agree with you.

Q88 Chris Philp: Does anyone else have anything to add on the question of the non-sign-off of the EU budget and whether we should be concerned?

Roger Bootle: I will just make a comment about the significance of this issue. First of all, as Professor Myddelton was saying earlier on, these are pretty small sums. I am going to take up with Philippe outside this room whether the figure is exactly £8.6 billion, as he said. I suspect it is one of these things where you can argue it lots of different ways but, if it is £8.6 billion or £11 billion, it is pretty small. I do not think that this issue of either the budget size or the misspending of the money—and there is a certain amount of misspending in Europe—should figure very large in this debate. Unfortunately, it does. It occupies a role in the popular debate about these questions out of proportion to the amounts in question. They sound like very large sums of money, but they are not really. 1% of GDP is about £16 billion, so we are talking, depending on who is right about the figures, about 0.7% of GDP or something like that. It is not enormous. The misspending of that money is not an enormous factor.

However, something else needs to be taken into account and that is my old friend the trends. What is going to happen to these figures over time? The likelihood surely is that if the EU goes on to form a closer union, and maybe even if it does not, the size of the common EU funds is going to get larger and, therefore, the size of Britain's contribution is going to get larger. The amount of money that, insofar as it is "misspent"—in inverted commas—is misspent, unallocated or unaccounted for is going to get larger as well, so I would not entirely dismiss it, but, as against the other considerations we have been talking about today—trade, for instance—this question of budget and misspending money or not being able to find it is small beer.

Philippe Legrain: There are a lot of ifs, buts and maybes there. The fact is that the Prime Minister negotiated a reduction in the EU budget for this five-year period. Potentially—God knows when—it might get bigger, but British agreement would be needed for that, assuming we are still in. As of now, the EU budget is smaller for this five-year period than the previous five-year period, thanks to the Prime Minister.

Simon Tilford: Good luck persuading the Germans and the Dutch to spend more money.

Q89 Chris Philp: I take the point that the panel are making, but I would remind you that we are currently trying to reduce our budget deficit. We just had an enormous wrangle over £4.5 billion of tax credits. To describe £8 billion as a trivial, inconsequential sum of money does not give due respect to the very difficult work the Government are trying to undertake to balance the nation's books. I would not want to dismiss any amount of money as being inconsequential or trivial. Certainly when running a business I never would.

Philippe Legrain: I did not say it was trivial or inconsequential. At the same time, you need to see what you buy with it. If, as a result of £8 billion, you buy access to the EU single market, which creates jobs and therefore tax revenues in this country, you are improving the budget position of the UK Government by being part of the EU.

Chris Philp: I understand there are pluses and minuses.

Q90 Chair: If I may just interject there briefly, we did begin this discussion with an examination of whether it was reasonable to use simplistic terms like "create jobs" as a result of membership of a particular trading agreement. Indeed, a little later on I thought we had got as far as agreeing that that was part of the lump of labour fallacy and that jobs would be created somewhere else. Do you want to change the evidence you began with?

Philippe Legrain: I spoke too quickly. Enhance the pay and productivity of British workers and the returns on capital of British investors, and thereby create higher tax revenues for the Treasury. I misspoke.

Q91 Chris Philp: I wanted to ask about, in your opinion, the effectiveness of the way the European Union spends its money, particularly with regards to things like the Common Agricultural Policy, which, by reputation, supports otherwise unproductive French farmers. I wondered if you could comment on whether you would agree with the thesis that some out campaigners advance that the European Union essentially spends its money unwisely, and that a more judicious Government or entity, such as the United Kingdom Government, might spend that money in a way that benefited our citizens more effectively.

Simon Tilford: The EU continues to spend too much of the budget on agriculture. The CAP has been reformed, but further reforms are necessary. I would like to see the emphasis placed much more on some of the energy issues, on facilitating the creation of pan-European energy networks and grids, for example, and much more on addressing some of the environmental and labour market issues in particular countries. I do not have a problem with the structural funds as such, although I think structural funds should be concentrated in poor areas. I do not think structural funds should be spent in wealthy areas. There is no point in the EU spending money in east Germany or the north of England. That expenditure should be renationalised. You need to reform structural funds, further reform the CAP and focus spending on things that will boost productivity in the EU. There is a whole host of things they could be doing. I do not mean subsidising R&D, but looking at research issues, the energy market and these kinds of things.

Professor Myddelton: I have been observing British Governments waste money for 50 years and more, so the idea that there is a huge difference between the EU wasting money and the British Government wasting money is a mistake.

Q92 Chair: Thank you very much for coming to give evidence to us this morning. I thought that last point was particularly provocative and one that this Committee will be looking at very shortly, when we look at the autumn statement. You have agreed to send us some more written evidence and, if you feel inclined to send us more than we have asked for, I think there is a market for it, on the basis of what we have heard so far. In one sense, we have got to the bottom of the issue. We have got to the bottom of how elusive it is to get to any concrete answer. On the other hand, in another sense, we have just scratched the surface of some of these very tricky problems.

I would just like to end by asking one mischievous question, which you are not obliged to answer. There will be a secret ballot when this referendum comes. Do any of you yet have a settled view on which way you will vote?

Professor Myddelton: I shall vote for leaving, as I voted in the 1975 referendum.

Simon Tilford: I know which way I will vote.

Philippe Legrain: So do I.

Roger Bootle: I am not absolutely sure. I think I am going to vote to leave, but I am sufficiently naive to believe that the Prime Minister might come back with something substantive. If he does, then I might vote to stay, but the chances of it are unlikely.

Chair: Those last four answers were also interesting and not necessarily clearly identifiable in some of the answers that you gave to questions, which only goes to show how objective you have sought to make the evidence to us this morning. Thank you very much for coming in to see us. It may not be the last exchange, orally or in writing, we have on this before we have to produce a report for the House of Commons.