

Treasury Committee

Oral evidence: [Budget 2016](#), HC 929

Thursday 24 March 2016

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Members present: Mr Andrew Tyrie (Chair), Mr Steve Baker, Mark Garnier, Helen Goodman, George Kerevan, Chris Philp, Rachel Reeves, Wes Streeting

Questions 115-266

Witnesses: **Rt Hon George Osborne MP**, Chancellor of the Exchequer, and **Clare Lombardelli**, Principal Private Secretary to the Chancellor of the Exchequer, HM Treasury, gave evidence.

Q115 Chair: Morning, Chancellor. Thank you very much for coming to see us. Another day, another witness. We have, in some respects, a rather curious Budget, in which you have adjusted the overall fiscal framework to take account of a change of less than £60 billion between these two huge variables, tax and spend. The average variation, according to the Office for Budget Responsibility over their forecasting period, is about £50 billion. You had a windfall only a few months ago of £27 billion, which you have spent. I just want to raise with you whether you think that it is prudent to carry on making these very short-term adjustments twice a year, rather than trying to set the achievement of the fiscal rule in 2020 in a longer-term framework, or a more medium-term framework. There seems to be very little economic loss to doing that—probably nil, since the variations that have taken place in the forecast are, as described by the OBR, largely noise, probably. However, there is a huge political cost and fallout, as we have just seen, to making these very frequent adjustments. Would you like to comment on that?

Mr Osborne: Yes. First, the overall Budget judgment is that we want to continue to repair our public finances and seek to try to improve our productivity, through measures on things like infrastructure and education. The Budget delivers that: the falling deficit, the surplus in the year 2019-20. If you go back to the Autumn Statement—and that was a time when I was setting out public expenditure plans through the Parliament—it would have been very odd, and I would have been rightly criticised, if I had delivered an enormous surplus in 2019-20; in other words, if all of the £27 billion improvement in the forecast had been put into surplus, I would have been carrying a £40 billion surplus, which is not what I have said is required. I have said that we need a sensible surplus, and I used the improvement in the forecast then partly to reduce borrowing but also to invest in capital and to make the public expenditure reductions less stringent.

Q116 Chair: If I may say, you spent it, basically.

Mr Osborne: No, £8 billion was used to reduce borrowing; £12 billion was one-off capital investment, so £20 billion of the £27 billion was not permanent structural increases in public expenditure, relative to where it might have been before.

Q117 Chair: This is not a current borrowing rule; it is a full borrowing rule, and so the investment point you are making is irrelevant.

Mr Osborne: Absolutely. I am very clear that you need the transparency of a simple rule around delivering an overall surplus, and that attempting to measure the cycle to estimate the output gap, trying to draw distinctions between capital and current spending, ultimately clouds that rule, as we have seen in previous Parliaments. That is the approach.

Underpinning all this is a set of independent judgments from the OBR. I was faced with an independent forecast that productivity growth in the UK—and indeed elsewhere in the western world, but obviously we are focused on the UK—was not as strong as previously had been expected. That is a structural deterioration in my forecast, and I thought it was sensible to act on that now with adjustments to public expenditure, albeit decisions that would take effect some years down the track, rather than waiting for events to come upon us. Indeed, “act now rather than pay later” is a political summation of a very central economic point I make, which is that Britain has to prepare itself for whatever the world throws at it, rather than react too late. Previous Chancellors have made their own assumptions about productivity growth and trend growth rate and been caught out, and here I have an independent judgment given to me and I act upon it.

Q118 Chair: I just come back to the question I asked, which was that you were describing it as a response to a structural adjustment, and the OBR are saying that the lion’s share of it may well be noise and that the average variation around the forecast is about £50 billion, and this adjustment is less than £60 billion. As I say, there was £27 billion moving in the other direction only three months ago, which rather makes their point. I am sure you have looked at what Robert Chote said about this. As usual, he was terribly careful to pick his words, but reading between the lines, it seems he is pretty much agreeing that you are locking yourself into quite arbitrary short-term changes with this. Is this an area on which you might reflect, given that you have already changed the charter that sets the overall fiscal framework for the Government three time last year, so it is not as if this is something that cannot be changed? We are talking here about a relatively minor adjustment in interpretation that might spare the Government a great deal of political grief.

Mr Osborne: I am prepared to take difficult decisions to try to improve the state of the public finances. I have set a clear target, which is that in normal times we will achieve a surplus. I have set a date for when we seek that to come into effect. The IMF, in its most recent article on the United Kingdom, went out of its way to praise the transparency and simplicity of our rule.

Q119 Chair: I am not challenging the rule, Chancellor. I am only asking how you are going to deliver it. I am asking whether it makes sense to make very short-term adjustments, twice a year, to fiscal policy to accommodate a rule that really boils down to saying that you are going to make sure you get a surplus by the end of the Parliament.

Mr Osborne: First, that is of course the rule to which we hold ourselves. As I say, there was a significant adjustment to the forecast since I presented the Autumn Statement. The independent OBR changed its judgment on productivity growth. You can do nothing about that. Previous Chancellors have been slow to react to changing information and evidence on productivity growth, and that has often led to significant problems down the track. It is best to get ahead of the curve. Partly because we have had a cautious and sensible approach, the adjustment does not have to be particularly large, but it does have to be adjusted.

Q120 Chair: Does “best to get ahead of the curve” not point to hanging on to the whole of the £27 billion last year?

Mr Osborne: Of the £27 billion that the forecast threw up, I used £8 billion to reduce borrowing and £12 billion was on one-off expenditure on capital, so the lion’s share of that money was used for one-off improvements.

Q121 Chair: We have been around that. It was really £19 billion that was made available for other purposes and £8 billion that was put aside, on a like-for-like basis.

Mr Osborne: £12 billion of that was one-off capital expenditure, so it did not lead to a structurally higher level of public expenditure.

Chair: Anyway, I am raising the issue that it seems to be a relatively straightforward thing to adjust this framework to reduce the scope for being hit by these rows. I leave the thought with you.

Q122 Chris Philp: Good morning, Chancellor. Just to continue on the Chairman’s line of questioning about the fiscal rule, some people in the House—not including me, I should add—queried the wisdom of reaching a fiscal surplus by the end of the Parliament. Could you just outline strategically why you think it is so important for our country to start running a small surplus from 2019-20?

Mr Osborne: Take a step back. When I became the Chancellor, the country was running an 11% budget deficit, which was the worst in its peacetime history. We have dramatically improved the fiscal position by reducing that deficit, but it does prompt the question of when you are ever going to run a surplus as a country if, after seven, eight or nine years of economic growth, you are not running a surplus. The same rule keeps coming around from my political opponents, which is a version of the current expenditure balance, and it essentially means a permanent deficit. I do not think that is a sensible way to manage the public finances. When the economy is growing and when we have repaired the finances from this massive deterioration, then in normal times—there is that flexibility—when the economy is growing at a reasonable pace, you should be running a surplus and using that to prepare yourself for whatever goes ahead. The fundamental premise of my approach is that we have not abolished boom and bust. You do not know what is coming next, so you need to be prepared.

Q123 Chris Philp: Good. In the House, shortly after you delivered your Budget statement, Ken Clarke suggested that had he been delivering the Budget he would have been slightly more hawkish fiscally. Clearly it is much easier saying that than doing it. What would your response to him be?

Mr Osborne: I talk to Ken all the time, and he is pretty robust on these things. You have to take this Budget alongside the Autumn Statement and the July Budget. We have had three fiscal events since the general election. What they collectively amount to is a significant fiscal consolidation. The OBR judge it to be the largest consolidation that the UK has undertaken, with the exception of the demobilisations after the First and Second World Wars. It is also the largest seen in the G7 for 50 years, so it is a very significant act of repairing the public finances, and I did not judge that we needed to go beyond what I set out in this Budget, and the OBR forecast bears that out. Ken was saying that I should have been more hawkish, but I think the mix is the right one. There will always be people who say you need to do more and there will always be people who say you need to do less.

Q124 Chris Philp: What did the IMF have to say about our strategy back in December?

Mr Osborne: They have said that it is absolutely the right strategy and that it is a textbook approach. We are cited internationally as an example of a country that is carrying out a significant and well thought through fiscal consolidation. It is borne out by the overall forecast for the UK economy, which has us growing faster than any other major advanced economy in the world, unemployment low and employment at a record high. These are uncertain economic times, there is a challenging international situation and we have a big challenge with productivity, so there are lots of challenges out there, but overall I sit here as a Chancellor with the fastest growing major advanced economy in the world, with record employment, and unemployment at 5%, and I am taking the steps now to try to maintain what we have achieved.

Q125 Chris Philp: I would like to move on to sugar tax. There has been some press speculation, I think prompted by some of the manufacturers, that either they might mount a legal challenge or they are urging the Government to rethink. Can you comment on the Government's position in response to those recent press reports in the last two or three days?

Mr Osborne: The first thing I would say is that many companies are doing the right thing, reducing the sugar content in their drinks, and that is to be applauded. Other companies are saying either that this sugar tax is not going to happen or that they are going to challenge it in the courts. I would say, if they want to have an argument about the sugar tax, bring it on. We are going to introduce a sugar tax. That is not a threat or a promise; that is the way it is going to be. It is the right thing for this country. It will make a huge improvement to childhood health, and it has been warmly welcomed across the political spectrum and also very much supported by the health profession and the education profession. We will now get on, consult on the technical details of the tax, although I have set out the parameters of it, and it will be introduced in 2018. It is introduced in 2018 precisely so that companies have two years to reformulate their products or change their marketing mix if they wish to do so. Otherwise, they will pay the tax.

Q126 Chris Philp: So any legal challenge will be robustly defended by the Government?

Mr Osborne: We first of all took legal advice before introducing it, and we are very clear that it is legal. We would of course robustly defend it if there was a legal challenge. However, I would say to companies, "Do not waste time and money on a legal challenge. Use this period to look at your products and see if you can reformulate." As I say, Robinsons, Tesco, Sainsbury's and the Co-op have all reformulated. These are products

for which the sugar can be reduced, and I would suggest that that is what we would like to see the industry do, but ultimately it will be up to them.

Q127 Chris Philp: Moving on to the stamp duty land tax, as you know I was a strong supporter of the 3% surcharge as a mechanism to encourage first-time buyers, although that is not a view the Chairman necessarily shares. I notice that the exemption for 15 properties or more was removed in the Budget, which again makes sense. For the Committee's benefit, can you just explain the rationale for that change?

Mr Osborne: We consulted on that feature when we introduced the stamp duty change. One of the features of stamp duty changes is that they are extremely market-sensitive, so unlike some other things the Treasury can look at, where you can talk informally to the industry, it is extremely difficult with stamp duty changes because of the market sensitivity and the legal constraints around that. When we announced a surcharge on stamp duty for additional properties, we wanted to make sure that we were not going to have an impact on the construction of new properties for sale and the like by larger developers, because obviously we want to see more homes being built. We said we would consult on whether larger purchases should be exempt. We have consulted and are satisfied that we do not need to have that exemption. Of course, a larger developer or purchaser would be able to use the commercial stamp duty property regime anyway, so that is why we made the change.

Q128 Chris Philp: Are you at all concerned by the relatively high proportion of non-UK residents buying new-build property in London, which in many developments is as high as 50%?

Mr Osborne: I am someone who wants the UK to be open to investment and to money coming into this country to support development, but I want to make sure that people who live in this country can afford to buy their own home. What I felt had got out of kilter was that the first-time buyer who has to put together a mortgage, which obviously can take time and requires resources, was essentially disadvantaged versus someone who just had, in many cases, cash to go and buy a property; it is not, by the way, exclusively foreigners who can do that. You have seen, in the buy-to-let market, a quite rapid increase in cash purchases.

We had already taken action on mortgage interest relief for additional properties—those are for traditional buy-to-let people—making sure it is just a fairer, more level playing field. For cash purchases, and many foreign purchases, it was not the case that that measure would affect them, so you get the additional stamp duty charge. It is just about giving the family who want to buy their own home or move home a better chance and a more equal, fair shot at purchasing that property. That needs to sit alongside other things, including stuff announced in the Budget, to make it easier to build homes.

Q129 Chris Philp: Speaking of the burgeoning buy-to-let market, the Bank of England's FPC commented that the very rapid growth in the buy-to-let sector is a systemic risk to the economy, and, as you know, they have called for powers of direction over buy-to-let mortgages to go alongside the existing powers of direction over owner-occupied mortgages. There is a consultation currently out, and it was referred to in a supplementary Budget document. Do you have any views you could share with the Committee on whether this is an

area you are minded to give the Bank of England's FPC powers of direction over, and, if so, on what timescale?

Mr Osborne: The short answer is yes. It is highly likely that we will give the FPC powers over the buy-to-let market. It is possible we are going to do that later this year. The measures I have taken in the last couple of fiscal events on additional stamp duty and changes to mortgage interest relief have been done in the knowledge that the Bank of England has concerns about a bubble emerging in this market. I am not saying that there has been any collaboration, because they are entirely independent, but I have informed the Governor of the Bank of England in advance of steps that I have decided to take in this space, so I think we have a coherent approach to that.

Of course, another big feature of the Budget was the Lifetime ISA. That is going to help first-time buyers, and no longer force them to choose between saving for their retirement and saving for their first home.

Chair: Have you got more?

Chris Philp: I could go on, but, in the interests of giving colleagues a fair crack, I will stop there. Thank you, Chancellor.

Q130 Chair: All in good time, on that last remark.

As I understand it, you said that you have taken these measures on the understanding that there is a bubble or that there might be a bubble, which the Bank of England is acting on or wants to act on.

Mr Osborne: The Bank of England's Financial Policy Committee has identified potential systemic risks in the large increase in the buy-to-let market, and that has been made publically available, so I am acting on that public observation.

Q131 Chair: You described it as a possible bubble that might be growing. If the bubble bursts, you will reverse the measures, presumably.

Mr Osborne: I do not think that would be necessary. The measures are sensible measures to level the playing field. Whatever happens in that market, you still have this situation whereby a person buying their own home has to put together the mortgage and the person with the cash purchase does not, so I just want to make it a more even playing field. By the way, we use the money, in this case, to help with community housing projects, so we are also supporting house production.

Q132 Chair: It is perhaps for another day, but it does not look to me like the housing market is much of a level playing field; it looks like one of the most congested fiscal areas in Britain today, with measures pointing in all directions at once, leading to extraordinary conditions in parts of the housing market around the country. I think you would agree that it certainly needs some attention.

Mr Osborne: I would say that the measures we have introduced have been aimed at helping families buy homes and imposing additional costs on people or institutions buying additional properties.

Chair: We might look at that another day.

Q133 Wes Streeting: Good morning, Chancellor. I want to take us back to the process and constraints under which you are operating in putting together the Budget. This has not been, I think everyone would accept, a happy process, and there is probably a risk that when President Obama visits next month he will think you have changed your name from Jeffrey to Bungle. In the process of the Budget, you talked this week about the lessons that need to be learnt or the lessons that you will learn. I just wondered what lessons you are taking away from this Budget, both in terms of the process that you went through but also the content.

Mr Osborne: I am very proud of the measures in the Budget to improve the productivity of the country, to invest in infrastructure and education, to tackle child healthcare, to lift lower-income people out of tax, and to deliver our manifesto promises. Obviously attention has, perfectly understandably, focused on the changes that were proposed to personal independence payments just prior to the Budget. Clearly, if we are going to make reforms to disability benefits, we need to go about it in a better way than we did, because they were intended to make sure that, in a rising disability budget, more money was focused on those who need it most, and that the disability benefit budget was well used, but it did not command support, as was perfectly obvious, so that is where the lessons need to be learnt.

Q134 Wes Streeting: One of my colleagues wants to come back in more detail on the welfare dimensions of the Budget, but thinking about the Budget in a broader context, one of the peculiarities is that the welfare debates dominated the Budget focus, but there are broader issues around economic policy and performance, and in particular the irony that your own targets are the ones that you seem to be missing. This week, in his post-Budget press conference and in front of this Committee, Robert Chote said that the surplus target in 2019-20 is being achieved because you are shuffling around tax and spending plans, and Paul Johnson from the IFS similarly said that the surplus in 2019-20 is achieved by simple movement of capital spending forward and corporation taxes backward. Are you only generating a fiscal surplus in 2019-20 because of accounting wheezes and window-dressing?

Mr Osborne: No, I do not accept that. That charge would be a fair one if the surplus then was forecast to disappear the following year, but it is actually forecast to be sustained, so there is both the achievement of the surplus and then maintaining that surplus going beyond that. I make no apology that we try to achieve a budget surplus in this country. That is perfectly sensible economic policy that can avoid us experiencing the kind of disasters that we experienced in the past.

Q135 Wes Streeting: There is a huge volatility, is there not, even in the space of time that has passed between the Spending Review and this Budget? The forecasts have changed to such an extent that it has created big holes for you to fill, so what confidence can we have that those numbers around 2019-20 will bear any resemblance to reality by the time we get there?

Mr Osborne: The world is a constantly changing place. Even since I have delivered the Budget, things have happened in the stock market, things have happened to the oil price and things have happened to gilts. The world economy and the British economy do not stand still in between fiscal events. The job of the Chancellor and the Government is to react to those events, set policy for the long term, and set objectives that we seek to achieve over the medium term, and that provides stability and confidence. Take a step back. I sit here as a Chancellor in a Government that has the fastest growing economy of

the major advanced economies in the world, we have close to full employment and we have unemployment at 5%. There are lots of challenges out there. I want to maintain that strength in the British economy.

Q136 Wes Streeting: Touching on the points the Chairman was asking about earlier, is there not a challenge that the self-imposed constraints that you have set yourself are driving behaviours in terms of decision-making in the Budget that have all sorts of knock-on consequences, some negative? For example, how can businesses plan for the future if taxes jump from year to year in pursuit of arbitrary targets that you have set yourself?

Mr Osborne: We have done the exact opposite, actually, when it comes to business taxes. At the beginning of the last Parliament I published what is called a business tax road map. At the beginning of this Parliament we have done exactly the same. We have set a long-term direction for corporation tax. I have set out reductions in corporation tax four or five years hence. That will help bring forward investment. I have made lasting changes in this Budget to the corporation tax regime, in terms of rates, reliefs, loopholes and the like that have previously existed, including changes that overturn 40 or 50 years of tax policy, by, for example, restricting debt interest as a relief in the tax system, or restricting the carrying forward of losses. That is a major reform, set out in detail, for the long term, and that is precisely why the UK continues to attract the lion's share of investment into Europe. It is precisely because we have that stable, long-term approach to business taxation.

Q137 Wes Streeting: Let us think about Robert Chote's assessment that you are shuffling around tax and spending plans, and think about the plights of some of your Cabinet colleagues. One of the striking things about Iain Duncan Smith's resignation letter, beyond the scathing remarks he has made about the fairness of the Budget and the challenges for the welfare budget in particular, is some of the observations he makes about the Budget-setting process. I will touch on two areas. First, he talks about his team and himself being pressured in the immediate run-up to a Budget or fiscal event to deliver yet more reductions to the working-age benefit bill, implying that it was not just this Budget; this is an ongoing problem ahead of Budgets or fiscal events. He also talks about the challenges that exist in order to meet the fiscal self-imposed restraints that he believes are distinctly more political rather than being in the national economic interest. Is that not a clear illustration that there is a problem arising from the targets that you have set yourself, which are driving a far more difficult challenge for Cabinet Ministers than may otherwise be necessary?

Mr Osborne: First, the objectives were set out in the Conservative manifesto, so they are very clear. The whole Government and the whole Conservative party signed up to them by standing on that manifesto. Secondly, as I have explained, they are essential to ensure stability in the economy. Thirdly, there is always going to be a robust process in the debate between the Treasury and big spending Ministries. There is nothing unusual about that. That has been going on for literally hundreds of years. You can read plenty of accounts in Governments of all colours of those robust discussions, but in the end you reach a collective agreement and that is the basis upon which the Government act or, as in the case you refer to, someone chooses to leave the Government, if they do not want to buy in to that collective decision. That is how, in the collective Cabinet decision-making, it should work.

Q138 Wes Streeting: Learning lessons, we know the Budget is signed off by the Cabinet, and Iain Duncan Smith was still a member of the Cabinet when that Budget was signed off. At what point did Iain Duncan Smith first raise concerns with you about your proposals for personal independence payment?

Mr Osborne: I do not want to get into, and I am not going to get into—I know you may ask me a number of questions about this—the private discussions I had in Government beforehand.

Q139 Wes Streeting: Did he raise it with you before he resigned?

Mr Osborne: As I say, I am not going to get into the private discussions we had. When it came to personal independence payments and disability expenditure, it has been clear from the Office for Budget Responsibility's forecast—not just this time but in the autumn—that the forecast expenditure was higher than had previously been anticipated. DWP undertook a public review of personal independence payments and DWP issued proposed changes, which have now been withdrawn. Those are all publicly known facts, but I am not going to get into the discussions that happened behind the scenes.

Q140 Wes Streeting: I am obviously not going to extract an answer, so let us then think about the consequences of recent events. The OBR stated that the abandonment of your plans for personal independence payment would reduce the surplus by £1.3 billion, but that this would not materially alter the probability of you hitting your surplus target. If you do not need to generate a £10 billion surplus to hit your surplus target, why were cuts to PIP in the Budget in the first place?

Mr Osborne: The proposals on personal independence payments announced in the days before the Budget by DWP were the response to a review that they had carried out—the so-called Gray review by Paul Gray. It was in the context of how we could better control the disability budget and how we could make sure that the money was going to the most disabled people, all within the context, of course, even with the changes, of an increasing budget on disability. They were examined on their own merits, and the observation that Robert Chote makes was that they were not material to the achievement of a budget surplus. They were discussed in the context of improving disability benefits.

Q141 Wes Streeting: I am slightly unclear, and maybe you can clarify, about whether the cuts to PIP were driven by policy factors, i.e. DWP thought that this was a good policy to pursue as part of their welfare reforms, or whether it was a decision driven by money and by budget—a Treasury-driven decision. I think most people looking on this externally will wonder, if the OBR said you did not need cuts to PIP to hit your surplus target, and if, as we have done this week, we have put a Budget through the House of Commons without plugging that hole, whether that reinforces the point that IDS made in his resignation letter, that these cuts were not defensible in the way that they were placed within a Budget that benefits higher earners. They were not necessary for the economy, were they? They were politically motivated.

Mr Osborne: Controlling welfare spending is necessary for the economy. One of the principal reasons why Britain's public finances ended up in a complete mess—

Wes Streeting: But what was driving cuts to PIP specifically?

Mr Osborne: I am going to answer that. You have to control welfare spending. There was a 60% increase in welfare spending under the last Labour Government, which was one of the principal reasons for the deterioration. At the same time, we want to make sure that those welfare payments are well targeted and help people. That is why we introduced personal independence payments, and the proposed changes, which we are not going ahead with, were within the context of a rising budget and an independent review that had been carried out.

Q142 Wes Streeting: I do not want to trample any more on detail on welfare. I just want to finish off by again looking at some of the consequences off the back of this. The other day, on the Floor of the House of Commons, I quoted back what Stephen Crabb said in his first statement as the new Secretary of State. He said that you will not be bringing forward plans for further cuts to the welfare budget. The Treasury line seems to be that there are no plans. “Will not” sounds a lot more emphatic, if I may say so. What is your view? Are you ruling out further cuts to the welfare budget for the remainder of this Parliament?

Mr Osborne: We are not going to seek further cuts to welfare, as you put it, or indeed any other measures to replace the £1 billion-plus that would have been saved each year from the personal independence payments measures. We do not have plans for further welfare reductions, and we are now going to focus on implementing the new Welfare Reform Act that has just passed through Parliament, which delivers £12 billion of savings to working-age welfare. As Stephen Crabb was making clear in the House of Commons, we are going to focus, when it comes to disability benefits, on making sure that they work as well as they should and on making sure the integration with our National Health Service and with our social services is effective, and that is the kind of long-term reform—which, by the way, was also flagged up in the DWP announcement just before the Budget—that we are now going to focus on.

Q143 Wes Streeting: Finally, on unfairness in the Budget, one of the other striking things about IDS’s resignation letter was the point that he makes when he says, “I believe the cuts would have been even fairer to younger families and people of working age if we had been willing to reduce some of the benefits given to better-off pensioners but I have attempted to work within the constraints that you and the Chancellor set”. Thinking about the longer-term interests of the country, and acknowledging the political factors that mean that all political parties do not want to touch benefits for pensioners or better-off pensioners, he has opened a debate. Will you now look at reducing benefits for some of the better-off pensioners, or are you ruling that out for this Parliament?

Mr Osborne: I am ruling out, for the Parliament, touching the pensioner benefits that we pledged to protect in our manifesto upon which we were elected.

Q144 Wes Streeting: Which ones are unprotected? Give us a list of which ones are not protected.

Mr Osborne: The three protected ones that come to mind are the winter fuel payments, the free bus passes and the TV licences. For the TV licences, in the next Parliament the responsibility has transferred to the BBC. When it comes to winter fuel payments, we have examined the case made by the Labour party in the last Parliament about whether to remove them. They were of course introduced by the Labour Government universally. The Labour party in opposition said, “Let’s remove them for the higher-rate taxpayers”.

As I am sure you know, only 3% to 4% of pensioners are higher-rate taxpayers, and the money saved would be between £100 million and £200 million. I am not saying that that is not a lot of money, but in the context of a welfare and pensioner budget of many tens of billions of pounds, it is pretty small, and the administrative complexity of doing all that just does not seem worthwhile to me. It was used as a fig leaf to pretend that large savings would come, but in fact very small savings, in the context of the welfare budget, would come from that manoeuvre.

If you look at what I have done, which has been criticised robustly from both political directions, I have limited the lifetime allowance for pension savings. You could save £1.8 million into a pension pot under a Labour Government; it is going to be £1 million under a Conservative Government. You could put over £250,000 a year into a pension under a Labour Government; now that is less than £50,000—£40,000. That got voted on on Tuesday. There is a restriction on the relief going to pensioners. I have increased the pension age, which was a difficult decision but exactly the kind of long-term decision that western democracies should be taking, and that the sensible ones are taking. That is going to save £500 billion.

I have taken a number of measures but they have all been designed to make savings in pensioner benefits without taking away from pensioners a decent and generous basic state pension, and I am extremely proud of the record in this Government of dramatically reducing pensioner poverty, which used to be a real scourge in the previous decades. A dramatic reduction in pensioner poverty is one of the great achievements of this Government.

Q145 Chair: Can we just return to Iain Duncan Smith's interview with Andrew Marr, which has been referred to? He makes a large number of allegations, but he makes two quite serious allegations, it seems to me. One is that DWP always opposed putting the PIP changes into the Budget. Is that your recollection?

Mr Osborne: The forecast for personal independence payments is, of course, part of the Budget in the sense that the OBR produce it, but the process that led to these proposals, now withdrawn, was born out of a DWP process that involved an independent review and a discussion, over many months, about what we could do to better target personal independence payments, which was indeed in the context, as Iain himself said, including in that interview, of recent court judgments that had gone against the Government. That was the context in which those discussions were had.

Q146 Chair: Just to be clear, it is not your recollection that DWP had always opposed this decision forming part of the wider set of Budget decisions?

Mr Osborne: It was a collective decision-making process, as evidenced by the fact that the announcement was made by DWP.

Q147 Chair: I am just trying to cut through the language to the answer. It sounds to me like it is not your recollection, Chancellor.

Mr Osborne: I have put it in my own words.

Q148 Chair: I think we can take that as: "It is not my recollection".

Mr Osborne: You can take it that I have expressed my opinion in my own way.

Q149 Chair: It is quite an important question. It is not absolutely crucial to the state of the world, but it is quite an important question. I think you are saying—correct me if I am wrong—that these discussions have been going on for many months and that the understanding that this might end up in a Budget and be part of the OBR arithmetic was well understood and accepted. Have I said anything that is incorrect?

Mr Osborne: There was a collective discussion that led to the DWP announcement. I am sorry that Iain left the Government. I worked with him over six years. It is always going to be a difficult relationship between the Chancellor of the Exchequer and the person in charge of the largest spending Department. That is what the jobs require of us. I am sorry that he has gone but I am proud of what together we achieved over six years to reduce poverty and inequality.

Q150 Wes Streeting: You have not addressed his charge that these were political rather than economic cuts. That is the lingering issue.

Mr Osborne: As I say, the announcements on personal independence payments were made in the context of the review that DWP had itself conducted into these payments.

Wes Streeting: That is not an answer to the question.

Chair: I do feel that we are some way—

Mr Osborne: I know you would like me to go into all the details of the private discussions I had in Government, but the truth is—

Q151 Wes Streeting: I just want you to answer what he said publicly, which is that these were driven by politics rather than economics. That is a public charge, not a private one.

Mr Osborne: Let me make it absolutely clear: I believe in collective government and collective decision-making, and we come to decisions and we make those decisions. If people do not agree ultimately with those decisions, they can resign from the Government and they can give their reasons, which clearly Iain has done. For those who remain in the Government, we will continue to carry on confidential collective decision-making. That, by the way, is the way that you have functional government.

Q152 Chair: I know other colleagues want to come in on this point, and I thought they would some days ago. I just want to ask about another aspect of his interview, which is related to what you have just said with respect to collective responsibility. He makes quite a serious allegation. He says, “I do think, genuinely, that there needs to be a greater kind of collegiate sense to the way decisions are made... You know, I wasn’t consulted on the Friday about those changes. I didn’t know anything about them until media started ringing me up and telling me. This is not the way to do government.” Is that something you recognise?

Mr Osborne: As I say, I do not want to get into the private discussions. My understanding—indeed, I gave some television and radio interviews after the Budget—was that we were going to take some months to get this right, and that is why I expressed myself in the way I did in those interviews. At the heart of all of this is whether you want to be working as a Government to try to control welfare spending. My argument is that, if

you do not do that and if you lose control of the public finances, the people who suffer are the poorest and most vulnerable in the country, and those are the people whom we are fighting for. They are decent hard-working people, people who have disabilities and people whom we want to protect. If you lose control of public finances and you lose control of welfare spending and you trap people in cycles of dependency, that is the greatest social injustice of all. That was Iain's insight. That is what I have worked with Iain on over the last six years, and I am very proud of what we have done together.

Q153 Rachel Reeves: Chancellor, regarding the interview on *The Andrew Marr Show* with Iain Duncan Smith, you made the point about the DWP consultation on disability benefits. What the former Secretary of State for Work and Pensions seemed to be saying was that he was worried and concerned that he came under pressure to put the consultation and respond to it before the Budget, and, "I'd always hoped that we would do this after the Budget so as not to get caught up with the Budget". The accusation he seems to be making is that, yes, this was a DWP consultation, but he wanted to respond to it after the Budget so that it did not get caught up in the numbers of the Budget, rather than rushing out a response. I think we all accept that this was a DWP consultation, but was there a debate or discussion about whether the response was before or after the Budget?

Mr Osborne: I know this is going to disappoint the Committee but I do not want to get into the private conversations I have in Government. It is self-evidently the case that there was collective agreement to publish the DWP paper on the Friday, or else it would not have been published.

Q154 Chair: So it is not fair to say that there was a lack of collegiality about the way that these decisions were being taken?

Mr Osborne: Iain has expressed his view and resigned from the Government; that again is self-evident. The DWP proposals in response to the consultation and review were published by DWP.

Q155 Chair: Before the reversal of policy took place on the Friday, was Iain Duncan Smith engaged in discussion?

Q156 Mr Osborne: There were certainly discussions taking place, including directly with him.

Q157 Chair: To what extent was the Prime Minister involved in these discussions?

Mr Osborne: They were principally discussions happening below the level of the Prime Minister but he was aware of what was going on, as he always is.

Q158 Chair: We have had a good canter around that. I just wanted to come back to one other point that Wes Streeting raised, which was about the shuffling around of the money in order to secure the surplus in 2020. That is not my phrase. It is a phrase of Robert Chote's in his question-and-answer session after he presented the OBR report. From what we can tell in his OBR report, he makes clear that it is not quite as straightforward as you suggested. In fact, this backend-loading problem of cuts is going to spill over into the next Parliament. You have said you are not shuffling money around because the surplus does not disappear in 2020, but it would pretty much disappear in 2020 if it was not for the fact that, as they put it,

£8 billion of further spending cuts, which some might call austerity, will be required in 2020-21. Has the OBR got that wrong, or have I got that wrong?

Mr Osborne: We have adjusted the total managed expenditure for the year 2020-21, but total public expenditure is still going up in real terms.

Q159 Chair: What you have said is correct but it is correct only because there is the spill-over of more public expenditure cuts in the next Parliament.

Mr Osborne: I would not put it like that. What I would say is that we have made—

Q160 Chair: I am only putting it like that because that is the way that the OBR has put it on page 8 of their report.

Mr Osborne: There are two charges here. One is that I have undertaken one-off measures to hit the surplus; that is the thrust of your questions. The second charge is, “Hold on; there are permanent changes.” I would say yes to the second charge. There are permanent changes. There is a permanent reduction in the growth rate of public expenditure in the following year, which would feed through into future years, and the savings we seek in the Government Departments are permanent structural improvements. We are making permanent adjustments to the OBR’s information that the productivity growth for the British economy is not what it was thought to be, and therefore, if you are going to cut your cloth accordingly, you need to make those adjustments to public expenditure.

Q161 Helen Goodman: Chancellor, one of your announcements was the reduction in business rates for small businesses, and that is widely welcomed, because I think everybody agrees that the burden on them has become too high. As you know, in this area of policy two things are going on. At the same time as you are cutting the business rates, you are also transferring the business rates over to the local authorities, so I would like to ask you why the transfer to the local authorities is not reflected in the Red Book table 2.1.

Mr Osborne: I read the session you had with Robert Chote, so let me first address that point that you are perfectly reasonably asking about, regarding whether local authorities are compensated for the reduction in business rates or the increase in business rate relief. The answer is yes, and that is reflected in the local government DEL in this Red Book. At the moment, local authorities retain 50% of their rates. That is a change that this Government have made and I am very proud of it. We are moving to 100% rate retention. The parameters of that were set out in the Autumn Statement; the details are now being worked through, including the redistribution mechanisms and the like. The reduction in business rates and the increase in business rate relief that I have announced will not affect that process nor mean the local authorities have less money.

Q162 Helen Goodman: I understand that you, and this has been repeated by David Gauke in the Chamber and by the Secretary of State for Communities and Local Government—

Mr Osborne: Collective decision-making; there you go.

Helen Goodman: You are all promising to reimburse the local authorities for the full effects. Unfortunately, the numbers in the Red Book do not reflect full compensation if you move to 100% retention by the local authorities.

Mr Osborne: The Red Book reflects, if you look at page 91 and local government DEL, the coming period of the forecast—the next few years—during which period you will not have 100%.

Q163 Helen Goodman: You will at the end of the time.

Mr Osborne: You will at the end, by 2020. We do not have public expenditure plans for that year. We do not have a local government settlement for that year and so on. That will all be reflected in the future. It is the case in this period, over the next five years, that the authorities will retain 50% of rates, and they are compensated for that, but I am also saying today that the reduction in rates, particularly on small businesses, and the increase in business rate relief will be reflected in the calculations we now make with local authorities over the coming years, and of course we are in discussion with a number of key authorities, like Greater Manchester and the GLA, about accelerating that process in some parts of the country, and it will be reflected in those negotiations as well.

Q164 Helen Goodman: Chancellor, do you not think that it would have been more honest to have included this extra cost of the transition to 100% in the Red Book? As you read the transcript, you will know the OBR, when they came to give evidence, did not know the answer to my questions. I looked at the table that they have published, which is table 2.43, published by the OBR, which is a breakdown of Budget 2016 policy decisions. It is not in the book; they published some additional things on the net. That shows that throughout the period they are assuming business rate retention at 50%, which is costing the Exchequer some £350 million. As you say, Manchester and London are going first, so there will be some extra cost to that, and at the end of the period there will be another £350 million cost, probably in your target year of 2019-20. You have missed out that £350 million from the Budget arithmetic.

Mr Osborne: We do not have agreement. That is not a negative thing. We are speaking to local government about the pace at which we get to 100%. Until you know the pace you are doing it, you cannot score the effects in a Budget.

Q165 Helen Goodman: So you think it is okay to have another £350 million that you know you are going to have to spend in 2020, which is part of the decisions and the policy as set out in the Red Book, not reflected in the numbers? You think that is all right?

Mr Osborne: There are many parameters in this extremely complicated but very important and radical devolving of business rates to local government, and this is one of the factors but there are plenty of others.

Q166 Helen Goodman: There are others, indeed. Have you thought, Chancellor, about the impact on the corporation tax liability of small businesses when they have a reduction in their business rate liability? What do you think happens to their corporation tax bill?

Mr Osborne: It comes down to an assessment for them to make. Corporation tax is levied on their profits, so if they had higher profits they would be charged tax on that. They can of course make investments and do all sorts of other things with that money. It is entirely a decision for the local business. The good news is that corporation tax is coming down.

Q167 Helen Goodman: Chancellor, the other thing that table 2.43, produced by the OBR, reveals is that the reduction in business rates leads to an increase in the corporation tax take

that you are going to make. You stood up in the Chamber and said there is a £7 billion cut to the nation's shopkeepers, but in fact that is not the case. The truth is, when you take account of the increased corporation tax they are going to have to pay, they are going to benefit only to the tune of £5.5 billion. £5.5 billion is a very large sum, I agree, but it is not a £7 billion cut to the small businesses. The small businesses are getting a £5.5 billion cut.

Mr Osborne: The OBR are making, as they are entitled to do, a set of assumptions about what small businesses will do with the extra resource that comes from not having to pay such high rates. The simple fact is that this announcement has been universally welcomed by all the small business groups.

Q168 Helen Goodman: Of course they have welcomed it. They have welcomed it and you told them that they were gaining £7 billion a year. The truth is that they are only going to gain £5.5 billion a year. That is a significant difference, is it not?

Mr Osborne: If you take an individual business, I have either reduced or eliminated business rates. There is more money in the business. What they choose to do with that money, whether they want to pay dividends—

Q169 Helen Goodman: They do not have a choice about whether they pay their corporation tax bill or not. That is not optional, is it?

Mr Osborne: Of course it is not optional. It is not optional because it is levied on the profits, but they can choose to do other things with that money. They could invest it in the business.

Q170 Helen Goodman: You set up the independent OBR, and all I am doing is telling you the numbers that the independent OBR are presenting. On the one hand, we have a £350 million extra gap at the end of the Parliament, and on the other we have the cut that you said small businesses were getting, which is not in fact £7 billion; it is in fact going to be £5.5 billion.

Q171 That brings us on to the question of whether the fiscal consolidation that you are promising in the Red Book is in fact credible. There are a number of items in here where you have not explained how you are going to achieve them. You have described £3.5 billion of resource spending adjustment and £2 billion a year of public service pensions, which will mean savings across the Departments. How do you think Departments are going to find that extra £5.5 billion?

Mr Osborne: First, £3.5 billion is a sum that I think the Departments can achieve. To put it in context, in the last year, after the general election, I undertook in-year savings in Departments that yielded £3 billion. I am asking for £3.5 billion from Departments in four years' time. That is all part of managing public expenditure. That is all part of trying to control the Government budget. If you are not prepared to make these decisions, it gets completely out of control. In terms of public sector pensions, we undertook major reforms of public sector pensions, which were completely unaffordable. Lord Hutton, a former Labour Cabinet Minister, set out proposals to reform those public sector pensions. One of the proposals that came out of that whole process was that every five years there should be an evaluation of the discount rate—

Q172 Helen Goodman: When did Lord Hutton report?

Mr Osborne: In 2011, I think. It is five years later.

Q173 Helen Goodman: So why were this resource spending adjustment of £3.5 billion in one particular year, your target year, and the public service pensions of £2 billion not incorporated into the public spending round and the Autumn Statement last year? Why have you just alighted on these things four months after your major public spending announcement?

Mr Osborne: We said that every five years—not every four years—we would conduct a review of the discount rate. By the way, if we do not do this, public sector pensions and the good pensions we pay to our public servants will become completely unaffordable. If you are running a public service, you have to employ the staff, you have to invest in—

Helen Goodman: Yes, I know that. I do understand that.

Mr Osborne: One of the costs of employing the staff is the pension that you pay. We are asking public sector employers to take into account that cost. By the way, there are swings and roundabouts because lower inflation forecast since the Autumn Statement has delivered a fiscal windfall to many Government Departments and public services.

Q174 Helen Goodman: Which you are clawing back with your resource spending adjustment of £3.5 billion, I suppose.

Mr Osborne: I am not clawing it back.

Q175 Helen Goodman: You are confident that they can find this £5.5 billion but you do not know how they are going to do it. Have you looked at how it will be distributed between the Departments, for example?

Mr Osborne: It depends on where the public sector pension liabilities fall, and we will work with the Departments on that. It is part of a complicated process, but there is an essential truth: what is the other body, apart from the Government and the Government Departments, that is going to pay the cost of public sector pensions and the changing liabilities? It is precisely because this kind of work was not done that the country was left in a complete mess.

Q176 Helen Goodman: Chancellor, you also have an unexplained £1.3 billion a year on PIP, which, as the OBR agreed with us earlier this week, you will have to find through further public spending cuts, higher taxes or extra borrowing. I have found another £350 million in the business rate transfer. That is another £1.6 billion unexplained in 2019-20. Obviously you have not decided how you are going to allocate these things in detail, but could you give us an indication: are you going to find this extra £1.6 billion through further cuts, higher taxes or extra borrowing? What is your sense of direction on this?

Mr Osborne: First, I do not accept, without revisiting it, your conclusions from our discussion on business rates.

Q177 Helen Goodman: You are surely not saying there will not be any cost at all to Government?

Mr Osborne: As I say, there is a discussion going on about business rates. When it comes to personal independence payments, all other things being equal, the forecast for disability

benefits and welfare will be just over £1 billion higher, but of course there are many other factors that go into a forecast on welfare, as you would well know. Robert Chote points out—I am quoting him—that it is not that large a sum in the context of other uncertainties. Already since the Budget there have been a number of things that will have an impact on the forecast for public expenditure and welfare spending, even in the space of a week, just because that is what happens in a complex economy. We will make an assessment, at the Autumn Statement, of what the public finances look like, what welfare spending looks like and the goals we have set out to achieve, and I am sure you will be in the Chamber when I set them out.

Q178 Helen Goodman: So you do not know and you have not decided. You are hoping that either you will find it down the back of the sofa or it will be lost in the rounding. Is that the message I am to take away from this?

Mr Osborne: The overall approach in the Budget was that the deficit should fall each year and that we should have a sensible surplus in 2019—around 0.5% of GDP. That remains the case. We will see what the world and the domestic economy throw at us in the coming months and then we will have an assessment at the next Autumn Statement.

Q179 Helen Goodman: The reason this is a problem is that, if we add all these things up together, it comes to over £7 billion in that year. It is £12 billion over the whole of the years covered by the Red Book, and the problem is, Chancellor, that all these are in the wrong direction for you. None of this is going in the right direction, so all this is putting at risk your hitting your £10 billion target, because it is not as if we have one thing going in one direction and another thing going in another direction. All the £7 billion is going in the wrong direction for you.

Mr Osborne: I am not sure I recognise that number. I could point out that, in the last week, equities are higher than the OBR forecast and the house price growth has been slightly higher than forecast; both of those things lead to increased tax receipts. There are plenty of things that go into a Budget forecast or an Autumn Statement forecast, and in that context the fact that disability spending will be just over £1 billion higher is—and I am only quoting directly Robert Chote—not large in the context of the other uncertainties.

Q180 Helen Goodman: Let me turn to distribution. Chancellor, on 22 March you said in the Chamber, “The truth is that that family and many more families are getting increased support under this Government”, and you said earlier in your session today that you were fighting for the poorest. Unfortunately, the suggestion that many families are getting increased support has not been borne out by the charts given to us and published by the Institute for Fiscal Studies. These show that the impact of tax and benefit reforms over the period from May 2015 to April 2019 is losses in annual net income for every single type of family apart from couples with no children and two earners. How do you justify saying what you said in the Chamber on 22 March, when the truth is that every single type of family, except for couples where both are in work and do not have any children, have lost money, and considerable sums of money as well?

Mr Osborne: I would say a couple of things. First, that IFS analysis assumes that every pound borrowed is a pound of gain to the families of Britain. I do not accept that at all. That is precisely what led to poverty and unemployment in our country when the—

Q181 Helen Goodman: Sorry, what do you mean by “every pound borrowed”?

Mr Osborne: The IFS analysis assumes that, if you reduce borrowing or reduce public expenditure, that is a loss to families. I would say that, if I went and borrowed, this year, £100 billion more, and I gave it evenly to the families of Britain, that would show up in the IFS analysis as a great win for the families of Britain. I can tell you that it would not be, because it would lead to an economic calamity for the country and a crash, and people would be poorer. That is the first point I would make.

Secondly, that IFS analysis is of decisions since the general election, I think I am right in saying.

Q182 Helen Goodman: This is the analysis that they have done on your Budget last week.

Mr Osborne: Yes, I have the analysis here. It does not include things like the national living wage, which is going to be a £900 pay rise to families in just a week’s time. By the way, if you read the IFS analysis published on 21 March, “Are we ‘all in this together’?”, it concludes, “In broad terms income inequality is lower than before the recession as increasing levels of employment have helped those towards the bottom of the income distribution”, and it says, looking at the income distribution, that in the years since the recession incomes have risen for those towards the bottom of the distribution and fallen for those towards the top.

Q183 Helen Goodman: Chancellor, I am not asking you at the moment about the whole range of this population. I am asking you about the impact of your measures, the things for which you are responsible.

Mr Osborne: Yes. Free childcare, a national living wage, an economic policy that has delivered a record number of people in work and rising real incomes are what the policies pursued by this Government are delivering.

Q184 Helen Goodman: I am sorry, but the tax and benefit changes that you have produced also mean that the bottom half of the income distribution have seen less than £20 of benefit, while the top half have seen £170. Between May 2015 and April 2019, the bottom half—

Mr Osborne: You voted for those tax changes on Tuesday. The Scottish National party divided the Chamber on the changes to income tax and you chose not to vote against them.

Helen Goodman: I am looking at the whole picture—

Mr Osborne: You had a choice. We all had choices. I made my choices. You made yours.

Q185 Helen Goodman: I am looking at the whole picture of what you did on tax and benefits. Your claim that families have gained is simply not true. The analysis that they have done shows—and they are completely independent, as you very well know, and they are highly respected—

Mr Osborne: That is why I am quoting them.

Q186 Helen Goodman: They show that the second poorest decile are losing £1,500 whereas the decile next to the top are gaining £170. That is what they are showing.

Mr Osborne: The IFS say that inequality is now at a 25-year low. If you had problems with the increase in the personal allowance and the increase in the higher-rate threshold, you could have voted against them. That is what Alex Salmond did, but you did not.

Q187 Helen Goodman: Sorry, Chancellor. This is a Treasury Committee inquiry. I am asking you questions. This is not about what I have or have not voted for. These are the questions I am putting to you about the way you have constructed your Budget.

Mr Osborne: I am comfortable with the things I have voted for. You seem a little bit less comfortable.

Q188 Chair: Helen, have one more go with one more question, and then I think we must move on.

Q189 Helen Goodman: Chancellor, you have said, and you have said it again today, that you devote your entire energy to fighting for the poorest. How can you square that with the fact that, when we look at working-age families with children, those in the second poorest decile lose £2,800, and those not quite at the top but in the second richest decile gain £500? How can that square with your claim that you are fighting for the poorest?

Mr Osborne: I point to the fact that inequality is down. There are 800,000 fewer people in relative poverty, 300,000 fewer children in relative poverty and 100,000 fewer pensioners in relative poverty. The country was in a complete mess six years ago, and people's lives, their livelihoods, their hopes and their opportunities were destroyed, and this Government, working as a team, have turned that situation around. People are earning more income, they are in work, economic security has returned to this country, and frankly if we had followed the advice that you and your colleagues have been giving us in recent years that would not have been the case.

Q190 Helen Goodman: Sorry, Chancellor, but the fact of the matter is the number of children living in absolute poverty has gone up by 500,000 between 2009-10 and 2013-14.

Mr Osborne: As I say, poverty is down—

Helen Goodman: It is not down.

Chair: Let the Chancellor respond.

Mr Osborne: According to the Institute for Fiscal Studies, which you have been quoting, incomes are rising for those towards the bottom of the distribution and falling for those towards the top. By the way, the IFS also point out that very high earners have paid significantly more tax, and I make no apologies for that; that is a fair approach. Inequality is now at a 25-year low.

Q191 Chair: Chancellor, there is a related problem, which is that part of the reason we are having this row is that you moved the goalposts with the distributional analysis that you published, did you not? The problem is that in 2010 you took a bold and I think excellent decision to reverse the decision of successive Chancellors for three or four decades, and you decided to publish high quality distributional analyses for the first time. When you restarted this process after the general election, you moved the goalposts of the distributional analysis so that it is very difficult to follow what is really going on for the same groups over time on the same basis. Will you go back, please, to at least publishing the distributional analysis on

the same basis that you did between 2010 and 2015, and by doing so greatly reduce the heat in the kind of exchange we have just had?

Mr Osborne: I do not remember the heat being greatly reduced when we did publish the information in the form that you set out.

Q192 Chair: On the contrary, there was much less heat about it all. We used to begin meetings by thanking you. I used to get criticised for thanking you too much for publishing this material, and often the hearing went right the way through without any discussion of distributional analysis, because you had set it all out and made it transparent.

Mr Osborne: I am merely observing there were quite robust discussions. I am very sorry to see that Mr Mann is not with us today. It comes back to the point I made about the IFS. The problem with the distribution we were publishing was that it assumed that all consolidation was a bad thing, and that attempts to reduce borrowing were a bad thing. In my view, that was too narrow a perspective. We have therefore published, as you are well aware, a different approach that shows the proportion of public services, which of course the IFS do not model, that go to the different income quintiles and in proportion of taxes, and what that shows is that, for the poorest people, they have received the same share of Government services, and the richest people have paid more in tax as a share of tax, and that is a fair approach to a fiscal consolidation.

Q193 Chair: By all means keep what you think is a fairer approach, but will you stick with what you yourself described as a very valuable approach, which was not just the approach that you took between 2010 and 2015 but also the fact that you were publishing it on the same basis every year, so people could see changes over time? Will you, responding to your own point that you have made repeatedly over those years, now agree in future to publish the distributional analysis on the same basis that you did between 2010 and 2015?

Mr Osborne: I am afraid I will give you the same answer I gave the last two times we had this discussion, which is that I think this is a better approach and this is the one we are going to stick with.

Q194 Chair: Without really adducing much evidence to show that it is.

Mr Osborne: Similar to the IFS approach, the other approach assumes that every pound extra that you borrow and distribute among the population is a good thing for those families. I do not agree with that because I think in the end, if you are not seeing the bigger picture, which is that your borrowing gets out of control, then that is a bad thing, and ultimately borrowing is deferred taxation.

Q195 Chair: Clare Lombardelli, you are responsible, presumably, for helping to put together this distributional analysis.

Clare Lombardelli: To some extent, yes.

Q196 Chair: Welcome to the hearing. I feel you need to be given an outing so I have finally thought of something to ask you—something that I cannot expect the Chancellor to know in great detail. This is presumably put together on the basis of what the Treasury have described as a microsimulation model. Could we have a look at the model?

Clare Lombardelli: Thank you for your very inclusive approach to the Committee. As the Chancellor has said, we think the way in which we do this is a better methodology for doing it. That is why we have adopted this one and that is why we are going to stick to it.

Q197 Chair: I will just have one more go. The question was: can we have a look at the model, please?

Clare Lombardelli: I am afraid I do not actually know the details of the model well enough to know the answer to that.

Q198 Chair: Chancellor, would you give some thought to that question? If you cannot think of a really good reason why we cannot have a look at the model, then publish it. If you can think of a good reason, put it on a piece of paper and let me know.

Mr Osborne: I suspect you might be disappointed with the answer but I am happy to reflect.

Chair: You mean you will put it on paper and it will not be a good answer?

Mr Osborne: I am happy to reflect on the request.

Chair: We are quite used to pieces of paper without good answers on them. We might come to a few more of those in just a moment.

Q199 Rachel Reeves: Chancellor, will you meet the welfare cap in any year in this Parliament?

Mr Osborne: That will be assessed at the Autumn Statement. Clearly, as was evidenced in the Budget, we are not currently meeting it, including with the proposed changes to PIP.

Q200 Rachel Reeves: At the moment I think you are off by £20.8 billion over the course of this Parliament. Obviously £4.4 billion of that is because of the changes to PIP, but even before that there was not one year in the Parliament where you were set to achieve the welfare cap. Is the welfare cap still Government policy?

Mr Osborne: The welfare cap is Government policy in the sense that it sets out the objective we have of controlling welfare spending and the level we had forecast to spend on welfare, and then, at the time of the Autumn Statement when the OBR make their annual analysis of whether we have hit it, we have to either comply with the welfare cap or explain why we have not, and do that before Parliament.

Q201 Rachel Reeves: Do you plan to take actions to meet the welfare cap?

Mr Osborne: We have to wait and get the assessment of what the situation is with regards to the welfare cap, and then we will either show that we have complied with it or explain why we have not.

Q202 Rachel Reeves: There is nothing in this Budget that will help you achieve the welfare cap. In fact, you have had to quite rightly abandon the one measure that would have brought you closer to it. If things continue like this, would you take action to meet the welfare cap, or would you prefer to explain why you have not met it?

Mr Osborne: That is a hypothetical. As you would well know, there are many determinants that go into a forecast on welfare. That is why there is an annual assessment of it rather than a monthly assessment of it.

Q203 Rachel Reeves: So you do not have a preference about whether you would rather explain why you have not met it or take action to meet it.

Mr Osborne: We will make that judgment at the Autumn Statement: whether we have complied with the welfare cap or, if we have not complied with the welfare cap, why we have not complied with it. That is a policy or economic judgment that we will make when we are in possession of the facts of the forecast.

Q204 Rachel Reeves: If you have not taken any actions in this Budget to move in the direction of meeting the welfare cap, and there are no other fiscal events before the Autumn Statement, one would expect the same verdict from the OBR to be given at the time of the Autumn Statement, because you are not taking any corrective actions, so I think it is fair to ask whether you plan to make further cuts or whether you plan to abandon this policy.

Mr Osborne: First, there are many determinants. The welfare cap provides a very welcome additional control on public expenditure. It is transparent. We are held to account for welfare spending. There was no control at all on welfare spending when I became the Chancellor. It was called annually managed expenditure but there was no management control at all, and the Treasury would spend a huge amount of time focusing on what the exact budget of the Wales Office was and have no view on what was happening to housing benefit, a budget many hundreds of times bigger.

This is a more sensible approach. I am held to account for it, as are my colleagues. However, many things go into the forecast for welfare. I will give you an example: last year, in the July Budget, lower inflation forecasts reduced the total welfare spending by £4 billion. There are many things, as well as policy, that go into the forecast for the welfare cap.

Q205 Rachel Reeves: The £4.4 billion shortfall in the Budget because of your decision to abandon the changes to personal independence payments can be met in one of four ways: through tax increases, spending cuts to Departments, further welfare cuts or more borrowing. Which one of those ways—because it has to be one of them, or a combination—do you plan to use to plug that gap?

Mr Osborne: You are trying to isolate one feature of the welfare forecast, which is personal independence payments rates or personal independence payments eligibility criteria. There are many other things that go into that forecast, and it is sensible to make an assessment when you have the annual forecast, which is done at the Autumn Statement. I have set out the broad objectives we are seeking to achieve, which are the reduction in the deficit and the surplus—

Q206 Rachel Reeves: Chancellor, the reason I ask about the £4.4 billion is not just picking one part of welfare spending; it was the biggest saving in the Budget but a few days after the Budget it had to be abandoned. That is why I am talking about that £4.4 billion number. I am not picking any other line from table 2.1 in your Red Book. This is something you have had to abandon because of the force of pressure upon you and your Government. It is only

right that you now need to explain where that £4.4 billion is coming from. It was an important part of your Budget. It was the biggest spending reduction, so I ask again: of those four things—tax increases, departmental spending cuts, welfare cuts or more borrowing—which is the way that you are going to plug that £4.4 billion gap in your Budget?

Mr Osborne: As I have explained, the forecast for public expenditure, for borrowing and for welfare spending will be made at the Autumn Statement. It will take into account many different things, including the fact that disability spending will be higher.

Q207 Rachel Reeves: But you made announcements in this Budget, not in an Autumn Statement, to further cut welfare. Of course you made other decisions in the Autumn Statement and in the Budget last summer to cut welfare spending, so you do use Budgets, as well as Autumn Statements, to make decisions about welfare spending. Without that £4.4 billion of savings, that leaves you a gap in this forecast period and this Parliament of £4.4 billion. Do you not know how you are going to meet that gap, Chancellor?

Mr Osborne: I know this is going over ground we have already covered. First of all—

Q208 Rachel Reeves: We have already covered it in that you have already, Chancellor, been asked the questions. You just have not answered them yet. That is the problem. That is why we are covering them again.

Mr Osborne: As I say, first of all, personal independence payments decisions were born out of a DWP review, and were about trying to make sure that the increasing money we spend on disabled people is well targeted and goes to those who need it most. That is the first thing. Secondly, I refer again to what Robert Chote, the head of the independent OBR, said. Given the average forecast errors over a four-year time horizon, a £1.3 billion difference is not large in the context of the other uncertainties.

Q209 Rachel Reeves: However, Robert Chote also said that you are going to miss the welfare cap by £20 billion during the course of that Parliament. I do not know about you, Chancellor, but £20 billion sounds like a pretty large breach of your own cap. Would you agree that £20 billion is quite a large breach of your own cap?

Mr Osborne: The assessment by the OBR is done at the Autumn Statement.

Q210 Rachel Reeves: Okay, then let us have a look at the Autumn Statement. At the last Autumn Statement it was also the OBR's view that you would miss the welfare cap every year in this Parliament.

Mr Osborne: I do not think that is the case. I think their view was that I would miss it in the first couple of years but not towards the end of the Parliament. That is the annual assessment that is done at the Autumn Statement.

Q211 Rachel Reeves: You did not take the measures to close that at the last Autumn Statement, so can we assume that at the next Autumn Statement you do not plan to take the actions to meet your welfare cap?

Mr Osborne: You can assume that I will make a judgment on the basis of the forecast, and either comply with the welfare cap or explain why I have not, which is what is required—or colleagues and I will explain why.

Q212 Rachel Reeves: In the Chamber on Tuesday, Chancellor, I asked about welfare spending and whether you would be making any further cuts during the course of this Parliament, and was told, “We have no further plans to make welfare savings beyond the very substantial savings legislated for by Parliament two weeks ago.” You are now saying that you will make a decision at the time of the Autumn Statement on whether there will be further cuts to welfare spending to meet your cap. Is that correct?

Mr Osborne: That is not what I am saying. I am saying that we make an assessment of Government policy on the basis of the forecast we see at the Autumn Statement. When it comes to welfare spending, I have been very explicit, as has my colleague, the new Work and Pensions Secretary, that we are not seeking to offset the £1 billion or so more we are going to be spending on disability benefits with some other welfare cuts. We do not have any other welfare cuts planned or in train. We are delivering the Welfare Reform Act and other stated Government policies that are publicly announced.

There are further changes coming to welfare, such as the migrant brake, which has been negotiated with the European Council, assuming the country remains in the European Union; we are not going to get into that, I hope, at this session, or else Mr Baker will have a whole string of questions for me. We have been very clear about our approach to this.

Q213 Rachel Reeves: Is it possible at the Autumn Statement, Chancellor, that you might make further cuts to welfare spending?

Mr Osborne: As I have said, we have no plans to make—

Rachel Reeves: That is not the question I asked, Chancellor.

Mr Osborne: I have said that we have no plans to—

Rachel Reeves: But, Chancellor, that is not the question I asked.

Mr Osborne: I have given you a very clear answer. We are not going to replace the just over £1 billion more that we are going to be spending on disability benefits with some other cut to welfare.

Q214 Rachel Reeves: With the greatest respect, Chancellor, that is not the question I asked. Is it possible at the Autumn Statement that you will make further cuts to welfare spending?

Mr Osborne: I imagine, if the country votes to remain in the European Union, that we will be seeking to make very good progress on introducing the welfare brake on new EU migrants.

Q215 Rachel Reeves: So it is possible that you will make further cuts to welfare.

Mr Osborne: We have no plans for further cuts to welfare.

Q216 Rachel Reeves: You just said that you had a further plan, Chancellor.

Mr Osborne: That is an announced plan. That is something that is publicly announced.

Q217 Rachel Reeves: So is it possible at the Autumn Statement that you will make further cuts to welfare spending?

Mr Osborne: As I say, we have no plans for further—

Rachel Reeves: That is not the question that I was asking, Chancellor.

Mr Osborne: It is the answer I am giving you, which is that we do not plan further reductions in welfare spending beyond the things we have already announced. We are going to focus on implementing the proposals that were in the Welfare Reform Act and indeed negotiated at a European level.

Q218 Rachel Reeves: I think anybody listening to this will have to conclude that it is entirely possible that you will make further cuts to welfare at the Autumn Statement.

Mr Osborne: That is not the conclusion I would draw from listening to me.

Q219 Rachel Reeves: So are you saying it is not possible that you would make further cuts at the Autumn Statement, Chancellor?

Mr Osborne: We are not planning further reductions in welfare. We are not going to replace the £1 billion extra that we are going to be spending on disability with some other welfare reductions. We have plans to introduce a welfare brake on EU migrants. That is what we are doing.

Q220 Rachel Reeves: Can you understand, Chancellor, why people might not trust politicians in general, and perhaps you in particular, if you refuse to answer what are pretty important questions, particularly for people who are reliant on these sorts of benefits?

Mr Osborne: People know what we have set out to achieve. It was in our election manifesto. This Budget delivers our election manifesto. That is what the country voted on.

Q221 Rachel Reeves: Your manifesto included a welfare cap, Chancellor, and people know, looking at the last Autumn Statement and this Budget, that you will not meet it by £20 billion unless you take further action, so if you want to implement your manifesto commitments, Chancellor, you will have to make further cuts to welfare spending.

Mr Osborne: The manifesto said that we would manage the public finances well, reduce the deficit, deliver a surplus and have a welfare cap, and that we would either comply with that or explain why we were not. We said that we would make £12 billion, as you well remember because it was a lively debate in the general election, in working-age welfare. The Act of Parliament that has just been passed will deliver that £12 billion.

Q222 Rachel Reeves: I do well remember it, Chancellor, because I remember at the time you saying that it would not be disabled people or children who would be paying the price, and yet since the general election we have seen that those are exactly the people who are paying the price of those £12 billion of welfare cuts.

Mr Osborne: I do not accept that.

Q223 Rachel Reeves: I will come now, Chancellor, to the letter that the former Secretary of State for Work and Pensions wrote to the Prime Minister on Friday. He said, “I have for some time and rather reluctantly come to believe that the latest changes to benefits to the disabled and the context in which they’ve been made are a compromise too far... They are

not defensible in the way they were placed within a Budget that benefits higher earning taxpayers.” Is there anything there that you would disagree with?

Mr Osborne: As I have said, I do not agree with my colleague, but I am proud that we worked together and I am sorry he has left the Government.

Q224 Rachel Reeves: Surely, Chancellor, you did agree, because after that, or after the Budget, you did drop the changes to personal independence payments. Presumably that is because you did agree with the former Secretary of State for Work and Pensions that, within that context, it was not right to make those cuts.

Mr Osborne: Those proposals, as I have explained, were born out of a review that DWP carried out, and these were the conclusions of that independent review. It was pretty obvious that it did not command much support, so we said that we were not going to proceed.

Q225 Rachel Reeves: You would concede, Chancellor, that the cuts to personal independence payments were not defensible in the way they were placed within a Budget that benefits higher earning taxpayers. Would you agree with the former Secretary of State?

Mr Osborne: As I say, they did not command support. They were the product of a review that DWP had conducted, and DWP announced the conclusions of that. We have not proceeded.

Q226 Chair: After the financial crisis of 30-something years ago—the 1979-82 period—it became a standing joke that, when any Government Department said that it had no present plans to do something, it must be about to do it. Having said that, I can well understand, frankly, that you are a Chancellor with a massive problem to deal with—a huge deficit—and no Government want to commit themselves more than they absolutely have to, which is why, although I am not going to reopen the exchange now, the ring-fencing, both on the spending and the tax side, seems to me to create a considerable constraint.

Mr Osborne: We are not working on any policies to cut welfare. We are, as the new welfare Secretary set out, looking at how we can better interact with the health service and with social services. That can reduce overall demand on welfare and welfare spending, but needs to be done in a way that does not change rates or eligibility criteria.

Q227 Chair: I am sure 30 years ago Geoffrey Howe was coming out with the phrase, “I have no plans to do something”, and I am sure whoever is Chancellor of the Exchequer in 30 years’ time—he or she is knocking around now somewhere—is already practising that line.

Q228 Mr Baker: If we could turn to some of the plans you have to make sure we are able to pay for all these benefits that you do need to cover, the OBR have revised down their forecast for trend productivity from 2.2% to 2%. Just to give your voice a break, Chancellor, perhaps I could ask Clare Lombardelli what the Treasury’s view is on why productivity is continuing to disappoint so far on from the financial crisis.

Clare Lombardelli: I suspect I might disappoint you on this one. The Treasury takes the OBR’s forecast, and it is for the independent OBR to make these assessments for the UK economy now, so we have handed this one over to them. That is their judgment, and, if you look through their document, they have quite a lot of detail about why they have made

this assessment. They point to the financial crisis as a time of structural break, if you like, and they put forward quite a lot of data that supports the analysis that they have made.

Q229 Mr Baker: They have, but I am looking for the Treasury's view of reasons for it, so that we can be reassured that the policy will deal with those reasons.

Clare Lombardelli: I understand that. What the OBR have put forward looks reasonable to us. In their assessment of how much weight you put on the more recent period versus the period going further back, the way they have done that seems perfectly sensible. We would not disagree with their analysis in that sense.

Mr Osborne: We have the option of not accepting the forecast. By accepting the forecast, we agree with it.

Q230 Mr Baker: Chancellor, you have a productivity plan, and there is plenty in it. It was the subject of debate on Tuesday. How confident are you that your productivity plan can get productivity up to the necessary levels?

Mr Osborne: I am not assuming, as previous Chancellors have, that you can lift the trend growth rate and then base your public expenditure plans off that. That is an error that befell this country just over a decade ago. I am optimistic that we can improve productivity growth in this country. Of course, it is growing. It was not growing some years ago. The OBR forecast that the rate of growth increases, but not as much as before. They point out that this is a challenge across pretty much all western democracies at the moment, and I think that what we are trying to do on education reform, infrastructure, devolution of the levers of economic growth to cities and counties and the like are all things that are addressing internationally identified weaknesses in the UK economy.

Q231 Mr Baker: We have an objective that we both agree on, which is that we should be the richest of all major economies by the 2030s. We would need a leap in productivity to accelerate past other countries, would we not?

Mr Osborne: It is a stretching ambition. I do not think there is anything wrong with having those sorts of economic ambitions. The big challenge will be the United States, because that is obviously a richer country. They have big challenges too, with productivity. Potentially we have more levers at our disposal than the United States. When it comes to other western nations, we are performing pretty favourably.

Q232 Mr Baker: Indeed. However, productivity growth is now expected by the OBR to be permanently lower. That increases the structural deficit. What I am really driving at is your level of confidence that our present productivity plans can deliver our ambition of being the wealthiest of those major economies.

Mr Osborne: I am optimistic, but I am not basing my public expenditure plans on that optimism. I am being more cautious when it comes to public expenditure plans. First, we have to make sure we are getting the right data. Charlie Bean, the former Deputy Governor of the Bank of England, very specifically has done a review to look at our productivity data. There are some odd consequences of the internet age; it is apparently the case, according to Dr Bean, that going into a travel agent to book your holiday is more productive than doing it online at home. That does not feel right and it just shows that the

way we measure productivity has not necessarily adjusted to changes in technology and patterns of society. That is the first thing.

Secondly, there is the fact that the OBR themselves say that this is a highly uncertain judgment on productivity, but they are being cautious.

Thirdly, you have what to me feels like the most plausible explanation, which is that across the western world the impact of the financial crisis and the allocation of credit has had major aftershocks for western economies, and of course we had a bigger financial crash than most, so you have that as well.

I guess the theory I reject, although it has some distinguished people who advocate it, is that somehow the ability of western societies to innovate has come to an end. This is the Robert Gordon theory. Personally, I think that is too pessimistic. The way modern technology is developing and the major changes in technology, in everything from renting out your house to getting a minicab, feel like productivity improvements to me, but they are not necessarily showing up in the data at the moment.

Q233 Mr Baker: In evidence to this Committee, Stephen Nickell articulated, perhaps without endorsing it, the idea that cheap credit has allowed firms to continue to operate that might otherwise have folded and led to a reallocation of capital, and that this is one of the explanations for why productivity has not continued to rise as we might have liked. What is your response to this idea that monetary activism might now be diminishing productivity?

Mr Osborne: That is a plausible theory. The question is about what drives it. It was not just the cheap credit; it was that the banks did not want to recognise losses on their balance sheets. The UK and the US made further progress in cleaning up those balance sheets and recognising losses than other nations did. The alternative would have been a much tighter monetary policy. That would have caused a huge amount of damage out there in the economy. It would not have been very creative destruction; it would have just been destruction, and people would have been unemployed.

The final point I make, which I suspect you would agree with, is that a loose monetary policy cannot be a panacea. It has to be a bridge to a more productive future. You have to use the space it gives you for the structural reforms that are going to make lasting improvements in our society, and I would suggest that what we put forward at the Budget does that.

Q234 Mr Baker: I suppose I would partly agree with you. The question is whether it is a bridge or whether it is a blow to the foundations; that is for another day.

What reply would you give to those who are suggesting that you should defer your consolidation plans and run a larger deficit for longer because of these problems? How would you reply to them?

Mr Osborne: I just think that is a big mistake. The reason why the UK has attracted investment and the reason why businesses have had confidence to start up in our country is because we have a credible public finance plan. People look at the UK and say, “They have got their act together”. Borrowing much more in deliberate and discretionary acts of public expenditure would be a big mistake. It has to be said that every time this approach has been put to the British people in the last six or seven years they have rejected it. It

feels to me like we are going to have a pretty similar argument over the next few years, and I suspect the British people will give the same verdict.

Q235 Mr Baker: Turning to the EU and the OBR, Clare Lombardelli, could I ask you to confirm that the OBR are required only to analyse the Government's stated policy, which in this case is to remain in the EU?

Clare Lombardelli: Yes, that is what Parliament has asked them to do.

Q236 Mr Baker: They did put quite a few words in their report on this subject. Do you think they had the right amount of analysis or too much?

Clare Lombardelli: That is a judgment for them.

Q237 Mr Baker: Chancellor, they came before us and they confirmed that you did not misrepresent them in what quotes you used. Would you accept that, in inevitably selectively quoting what they said, you did draw the independent OBR into the EU debate?

Mr Osborne: No, I do not accept that.

Q238 Mr Baker: For what reason, then, did you quote them in the course of the Budget speech?

Mr Osborne: I thought it would have been very odd to give a Budget speech and not to mention what the OBR were saying about the EU.

Q239 Mr Baker: Do you accept what the OBR said: that it is not for them to judge whether we should remain or leave?

Mr Osborne: I explicitly said that in my Budget speech. To quote a line from my Budget speech, "The OBR correctly stay out of the political debate and do not assess the long-term costs and benefits of EU membership", but you will be glad to know that the Treasury is going to be doing that.

Q240 Mr Baker: I will come on to that in a moment. Do you think it might have been wise, to deflect the criticisms of me and my colleagues in the campaign to leave, if you had also made reference to the potential benefits of leaving the EU?

Mr Osborne: They cited a number of studies. You can read what they say about that. They were very clear in their conclusion that "there appears to be a greater consensus that a vote to leave would result in a period of potentially disruptive uncertainty while the precise details of the UK's new relationship with the EU were negotiated". Of course, I did note that Robert Chote said that I did not misrepresent them.

Q241 Mr Baker: Indeed, yes, as I said. You mentioned the Treasury's forthcoming analysis of costs and benefits, which you will realise I am looking forward to with great enthusiasm. Will the OBR be providing any kind of independent analysis or assessment of that report?

Mr Osborne: No.

Q242 Mr Baker: Do you think you might accept any arguments that perhaps they should since they have been established to give an independent perspective on policy?

Mr Osborne: You can ask them. I do not know whether they would want to or not. The Act of Parliament that established the OBR was clear that they could not examine alternatives to Government policy.

Q243 Chair: Chancellor, you or somebody has briefed the press that you are going to publish this analysis in May. Is that correct?

Mr Osborne: It will certainly come before the purdah for the referendum.

Q244 Chair: What we want to know is how far before the referendum.

Mr Osborne: When we have the date I will let you know.

Q245 Chair: No, we are going to pursue it now, for some time if necessary. This is not acceptable. This analysis needs to be subjected itself to thorough investigation by those on both sides of the debate.

Mr Osborne: To cut to the chase, I think you are likely to be able to examine me on it when I next come before the Committee.

Q246 Chair: When are you going to publish this document?

Mr Osborne: We do not have a firm date, but, as I say, it is likely to be published before I next come before this Committee to discuss all things European.

Q247 Chair: When you next come before us it will be on Europe. We will want to have had some time to digest that document before you appear. Are you going to give me a commitment that we are going to have, let us say, at least four working days prior to your appearance to enable us to look at the document? I am very grateful for the guidance that you have just given, which is helpful by the way, so I am pocketing that and am now trying to establish—

Mr Osborne: To be honest, I am trying to remember what date I am coming before this Committee. They are very exciting moments in my social calendar, but unfortunately I have forgotten the next one.

Chair: It is 19 April.

Mr Osborne: I think you will have had time to digest what has been published.

Q248 Chair: So it is going to be published in the first week back, is it not?

Mr Osborne: No. As I say, there genuinely is no date agreed yet.

Q249 Chair: Is it written?

Mr Osborne: It is being written.

Q250 Chair: You have had plenty of time to write this document, Chancellor. It is not as if there have been great changes in the kinds of questions you need to look at.

Mr Osborne: I think it is going to be a very good document when it comes.

Q251 Chair: We have made some progress. We are going to get a document sometime in the first fortnight of April and certainly with some clear water before the 19th. I suggested four working days as a minimum to enable us and our staff to take a look at it. I am extremely grateful to you for that. It is a good step forward.

Mr Osborne: The alternative would be to change the date of my appearance. I will undertake that there will be at least four working days before I come before this Committee, and you will have had a chance to examine the document and think about the kinds of issues you want to raise with me.

Chair: We will change that date with great reluctance.

Mr Osborne: I am sure you will.

Q252 Mark Garnier: Chancellor, good afternoon. I want to talk about household debt, but before I do so can I just carry on with the distributional analysis of the Budget? I want to focus very specifically on the raising of the tax-free threshold, which of course is a manifesto pledge that half of this Committee got elected on the back of. Nonetheless, focusing directly on that, it is no longer benefiting the poorest in our society; it is now benefiting the second decile. Have you considered an alternative to this, which would be, rather than increasing the starting rate of tax, increasing the starting point of national insurance, which, paced at the right level, would have no extra cost to the Exchequer but would help the bottom decile? Is that something that could be done?

Mr Osborne: Of course it could be done, and it is one of those tax decisions that you can examine at every Budget. However, we made a manifesto commitment on the personal allowance: to take it to £12,500. I would say that tax is not the only instrument. One of the challenges with the IFS distribution, without getting back into all that, is that that is a distribution of all households, not of all taxpayers. If you reduce income tax, those are reductions that go to income tax payers. We have taken 4 million people out of income tax, which is something that we are very proud of. We will deliver on the manifesto commitment. We keep other taxes like national insurance under review, and there are other instruments available to us, such as the national living wage.

Q253 Mark Garnier: Getting back to the savings ratio, it is now at a very, very low level. I think it is at the lowest level on record, at 4.4%. If you take out pension equity adjustment, we are at a negative savings ratio. If you look at some of these other charts with the OBR, and you look at household net worth relative to household income, you see that household net worth is going up, as we see house prices, apart from anything else, going up. Household debt is also set to rise, according to the OBR. It is about 145%, expressed as a percentage of household income, and is set to go back up to close to 170%. Do you, as I do, sense that some of these things that are coming up in these charts and these predictions have a certain element of what we were seeing in the run-up to the financial crisis? We saw a very sharp spike in household debt, in nominal terms and percentage terms. Do you have any concerns that we are beginning to build a few imbalances within the economy that may start precipitating a problem?

Mr Osborne: We should certainly be extremely vigilant to avoid a repeat of what happened. One of the biggest public policy innovations that I have introduced over the last six years is one that gets some of the least coverage: the creation of a Financial Policy

Committee in the Bank of England with real macroprudential instruments to, for example, change mortgage standards. Parliament has chosen to give this committee very considerable power as a result, to change things that have a direct impact on people's incomes, their ability to purchase houses and the like. That Financial Policy Committee is charged precisely with this task of identifying potential bubbles or balances emerging and taking action, to use the phrase, to remove the punch bowl when the party gets going. That gives me reassurance that we are in a much better place than we were seven or eight years ago.

The other thing that has happened is that UK households have de-levered much more than in most other western countries. I think we have had the second largest de-leveraging of any of the G7 economies. Even on the savings ratio, which of course is lower, as often happens as you get recoveries from recessions—the savings ratio falls—the OBR themselves note that that is a net number, and they say that, while consumption grows slightly faster than household disposable income, this is offset by rising pension savings as auto-enrolment coverage and contribution rates increase. The savings ratio is a net number but the volume of pensions savings is increasing. Again, one of the least talked about public policy successes we have had is auto-enrolment, which has created millions of new pensioners.

Q254 Mark Garnier: Absolutely. The OBR note that the household sector, in order to make the economic numbers balance, is required to have a deficit to the tune of 3% of GDP over 2016 to 2021. It also notes that this is an unprecedented level of household deficit. I had an interesting conversation with the Governor of the Bank of England when he first arrived. I was asking him about household debt and how he felt about this, to which he made a less heartening comment than he would make now. He has changed, but he said that, as far as he was concerned, monetary policy was his job; social policy and trying to protect people was the Government's job and the policy-makers' job, and therefore he would just go and raise interest rates willy-nilly. That was the implication he was making then. I might add he has completely changed since then.

Nonetheless, it is very difficult. There is a tension in the economy: on the one hand, we have households that are being increasingly stressed; on the other hand, we do need household consumption in order to help the economic recovery. Again, this puts policy-makers in a very, very difficult position. How do you square that circle?

Mr Osborne: I do not really accept that deterring savings is a good thing for economic policy; it is an approach of, "Make me virtuous but not yet". The measures that I have introduced on pension flexibilities, the increase in the ISA limits and the introduction of a Lifetime ISA are all policies designed to increase saving, even if some economists would say the short-term imperative is to increase consumption. It is right that you want to be trying to increase saving in our economy and I have set out a number of policies to try to achieve that.

Q255 Mark Garnier: Another conversation I had very recently with the Governor was a European discussion looking at the 2014 Bank of England stress test, which created a rather interesting so-called doomsday scenario, although actually the elements of this doomsday scenario as individuals were not black swan events; they were events that could happen. It basically painted a scenario where you would see a decline in consumption and a panic in sterling, which would result in an unwelcome rise in interest rates, so not one precipitated by

strength in the economy but precipitated by sterling crisis. You would see import inflation, you would see a tightening of credit conditions, you would see the housing market collapse, and you would see all sorts of different problems. In this particular stress test, the precipitation of this was a lack of confidence in productivity. It is a slightly cheeky question: can you see, over the next few months, anything coming up that could potentially precipitate an economic shock that would perhaps be good to try to avoid?

Mr Osborne: I suspect that this will be the subject of considerable discussion when I come before the Committee in April on European issues. I am very clear that our exit from the European Union would cause an economic shock, or a convulsive shock, as has been described recently. That would have an impact on prices and GDP and the like. That is not just my judgment; that is a judgment expressed by a whole range of independent observers of the British economy who have no skin in the game, as they would say.

Q256 Mark Garnier: So Government policy is such that we should avoid taking risks that could cause—

Mr Osborne: Government policy is to recommend to the British people that they vote to remain in the EU for a whole host of reasons.

Chair: We are going to have a quick canter around this on 19 April, we hope.

Mark Garnier: I have strayed away from the Budget. Thank you, Chancellor.

George Kerevan: Good afternoon, Chancellor. Thank you for staying.

Mr Osborne: I did not have many options.

Q257 George Kerevan: We would not have sent you to the tower. The Budget places a heavy emphasis on infrastructure. This morning on the BBC *Today* programme, the Secretary of State for Energy and Climate Change was questioned about the Hinkley C nuclear project, which is possibly our largest infrastructure project. She was at pains to say that the construction risk for the two Hinkley C reactors falls squarely on EDF. Surely under the UK Guarantees scheme for infrastructure, which you brought in, EDF has been given construction guarantees for Hinkley. Could you confirm that, and could you explain the detail of those guarantees?

Mr Osborne: I do not have the detail of the guarantees in front of me but I am very happy to write to you on the detail and set out the overall objective of those guarantees.

Q258 George Kerevan: But they have been given?

Mr Osborne: There are infrastructure guarantees that help with things like the financing of the project, but the central protection that the UK taxpayer has in the Hinkley contract is that if the plant cannot be made to work—in other words, if they cannot build it or the reactor design is not effective—the British taxpayer is insulated and protected from that. Construction risk and technical risk are absorbed by those building the plant, not by the UK.

Q259 George Kerevan: I have here before me the UK Guarantees scheme for infrastructure assessment, as done by the National Audit Office last year. It details that the scheme “enables the Treasury to issue an unconditional and irrevocable guarantee to the lenders of

infrastructure projects”—unconditional and irrevocable—“ensuring that scheduled interest and principal payments will be paid in full, irrespective of project performance”, which must involve, in this case, whether the reactor works or not. The National Audit Office goes on: “This transfers project risk to Government and ultimately taxpayers”. As I understood it, when you were in China last autumn, you negotiated and signed off on a construction guarantee. If we are taking the words of the NAO, we have transferred to Government and ultimately to taxpayers, as I understand it, £2 billion of risk.

Mr Osborne: Again, taking a step back, we are seeking to do what I think no other country in the world has done, which is to have a nuclear power station built off the Government balance sheet, without the taxpayers being involved in the construction risk associated with that. The infrastructure guarantees address weaknesses in the financing and funding markets; it is not the construction risk. They are designed to protect against failures in financing, not failures in construction—for a fee, by the way.

Q260 George Kerevan: I understand it is for a fee. At what point would that guarantee be triggered?

Mr Osborne: Unfortunately I do not have the details in front of me, but I am happy to write to you about that, or to take a couple of questions when I next come before the Committee.

Q261 George Kerevan: Pursuing that just a little, as I understand it, the infrastructure guarantee scheme is capped at £40 billion.

Mr Osborne: That is a controlled total that we have announced.

Q262 George Kerevan: Understood. The scheme is controlled within the Treasury. Treasury officials have undertaken pre-qualification negotiations with possible users of the scheme to ensure that the money could be allocated fairly. The pre-qualification negotiations resulted in £17 billion of the £40 billion being set aside for Hinkley. Is that correct?

Mr Osborne: Yes, from recollection.

Q263 George Kerevan: £17 billion out of £40 billion suggests that you are prepared to underwrite a huge risk.

Mr Osborne: As I say, the infrastructure guarantees address weaknesses in financial markets when it comes to infrastructure projects. What we have discovered with the infrastructure guarantees is that they have not been called upon and actually they have often prompted improvements in the project that have meant that they are not even needed, so we have actually underwritten many fewer of them than we expected. I think we are mitigating the financial risk and construction risk that is inherent in the construction of nuclear power stations in the way that we have approached this, and that shields the taxpayer from the kind of risks that they face in other countries.

Q264 George Kerevan: The NAO says it transfers the risk. I take the point that it is a guarantee scheme and it is not always called upon, but previous guarantee schemes have been called on big time, such as for the Channel Tunnel and HS1; the UK Government had to underwrite a guarantee scheme that was offered to that. The Department for Transport had to pay out £4 billion or £5 billion, so they are called upon.

My next question follows on from how we are identifying where the risk might fall and how we may have to pay. As I understand it from the National Audit Office's assessment, the scheme is available at all stages and is irrevocable. I read that to mean that, in a hypothetical situation, EDF could be refinanced with a loan from the French Government, begin construction, then refinance that loan with your guarantee in the markets, pay off the French Government, and leave the UK taxpayer underwriting the risk of the project being finalised. Is that true?

Mr Osborne: I do not think that is the approach that will be taken.

Q265 George Kerevan: But it is possible.

Mr Osborne: I am not sure it is possible, actually, as part of the final investment decision that will be taken. Again, I am happy to provide a written response to this, and indeed, with Mr Tyrie's forbearance, to take a few questions on this at the next session.

Q266 George Kerevan: That is very good of you. Thank you, Chancellor. I have a final point, just to complete where I am going, so you can add it into your letter. The NAO did a very interesting exercise comparing the cost to the taxpayer of the construction of all the projects under the guarantee scheme, including the full £17 billion for Hinkley, with what it would be if that had been paid for simply by Treasury borrowing directly, putting in the money and paying for it. The guarantee scheme ultimately adds a cost, because if the companies go to the bond market, because bonds are less liquid, there is a risk premium. In this guarantee scheme report, published last year, the NAO found that it was costing £180 million more per year, over the lifetime of these projects, which comes to many billions, than the Treasury simply borrowing the money, issuing its own paper and doing it that way.

Q267 That £180 million extra doing it this way, annually, of course ends up in the capital cost of the project, which is then passed on to the consumer. Given that you have agreed to underwrite the Hinkley operation, if it ever becomes operational, by giving it a strike price twice the current consumer price of electricity, that suggests that the guarantee route that you have entered into will almost certainly guarantee that the consumer pays more if the project is finalised.

Mr Osborne: I do not accept that for these reasons. First of all—

Q268 George Kerevan: You do not accept the NAO numbers?

Mr Osborne: No, I do not accept the conclusions that you draw from them. The first reason is that you are assuming that the British Government would be capable of building, on time and on budget, this nuclear power station. EDF, as is patently obvious from the report—

George Kerevan: Has no track record of delivering on time and on budget.

Mr Osborne: It is having challenges with the reactor at Flamanville, and indeed the reactor in Finland. We have undertaken this project off our own balance sheet. We would be facing very similar challenges to those that that company is facing with its French reactor. We are insulated from that and we can allow them to try to sort those problems out, which they are doing, and I am confident that they will reach a point where we can have a final

investment decision from them, and I think that they will be very good partners for this project. That is the first thing: the taxpayer is insulated from the construction risk.

Secondly, on the strike price, a few weeks ago there were plenty of reports saying, “The British Government has struck a deal where the guaranteed price is three times the market price”, but, as you have just said, now people are saying that it is twice the market price. In other words, the market price changes a lot. The oil price has gone up by 50% in the last two or three weeks. We are trying to build a nuclear power station that is going to provide base-load, low-carbon electricity, reliable at all times of the day and night, with wind speeds and weather conditions and whatever, and it is going to do that for decades, so it is a bit narrow in the analysis to say, “This is the oil or electricity price today. This is the price you are prepared to pay in the future.” We are trying to provide secure guaranteed electricity that amounts to 7% of the entire UK electricity demand from this one power station, going forward.

Of course, you can have a debate about whether or not the country wants nuclear power, but I have not seen a convincing alternative way to have low-carbon, reliable base-load electricity going forward. You can have as many wind turbines as you like, or you can have as many gas-fired power stations as you like, but you are not achieving that objective of low-carbon, reliable base-load electricity generation. The country that started the civil nuclear power programme in the world should not give up on it.

Q269 Chair: What about somewhat lower carbon but low-cost? Then you can go for your gas-fired generation, which is coming in much, much cheaper than Hinkley Point, at £92.50 per megawatt hour.

Mr Osborne: It is at present, if you take today’s gas prices. Mr Tyrie, you are a student of history. If you can assure me that there will be no fossil fuel energy crisis in the next 30 or 40 years, and that the UK can always rely on cheap and plentiful supplies of gas and should put all its eggs in that basket, then fine, but I suspect that you do not take that view. The best thing is to have a mix. We have had 20% of our electricity provided by nuclear power stations all of my lifetime, and it would be a mistake to give up on nuclear power, not, as the French have done, as the predominant source of our electricity, but as an important, reliable part of our electricity.

Q270 Chair: How closely has the Treasury been involved in analysing the choice between different types of nuclear power and different types of power station? After all, there is another controversy, quite independent of the points you have just made, about whether Hinkley Point has the right technology.

Mr Osborne: The Government have—

Q271 Chair: It is really how much the Treasury has been involved.

Mr Osborne: We are not a nuclear design authority.

Chair: You now have this infrastructure group. To be more precise with the question, what I want to know is whether you are treating the decisions about technology as a black box with an answer emanating from another source, or whether you are investigating that in depth from within the Treasury using Treasury resources.

Mr Osborne: The Treasury does not make an analysis of nuclear reactor designs. Our approach, which was set in train under the previous Labour Government, has been to identify opportunities for nuclear power stations, at Hinkley, Bradwell, Wylfa in Anglesey and so on, and then ask who can come forward with a project that is financeable and that will provide the electricity required. It has to be commercially viable for the project to succeed, but also, in terms of safety and the like, we have an authority that signs off on the design.

Chair: Chancellor, we have been going a little over two hours. We are very grateful to you for coming to give evidence. There has been the occasional uncomfortable exchange, as you would expect. Chancellors are not appointed to be popular, and, in any case, if you are bequeathed the largest deficit and the worst fiscal inheritance in the whole of British history it is quite likely you will have to take some extremely tough decisions. We look forward to seeing you in mid-April after having had a chance to read the Treasury's analysis of the costs and benefits of membership of the European Union. Thank you very much for coming.

Mr Osborne: Thank you.