HOUSE OF COMMONS

# Treasury Committee

## Oral evidence: The work of the Chancellor of the Exchequer, HC 777

Wednesday 19 October 2016

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Watch the meeting

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

Questions 1-114

### Witnesses

I: Rt Hon. Mr Philip Hammond MP, Chancellor of the Exchequer, Mark Bowman, Director General, International and EU, HM Treasury.

### Examination of Witnesses

Rt Hon. Mr Philip Hammond MP, Chancellor of the Exchequer, Mark Bowman, Director General, International and EU, HM Treasury.

Q1 **Chair:** Chancellor, thank you very much for coming to give evidence to us this afternoon. Of course we will be seeing you again before the end of the year to discuss the much-awaited Autumn Statement, which will reset economic policy. I would like to begin by asking about the letter that appears to have been leaked, or at least partly obtained, by "Channel 4 News" about migration and your views on student migration. Are you winning the argument on this: that students should be excluded from the total?

***Mr Hammond*:** I cannot discuss a leaked document today. However, as we approach the challenge of getting net migration figures down to the tens of thousands, it is essential that we look at how we do this in a way that protects our economy and the vital interests of our economy. It is the case that student visas have been abused in the past. The previous Home Secretary did some sterling work in tightening up on bogus educational institutions.

Q2 **Chair:** We are talking about people coming here for legitimate reasons, to study recognised courses. Are you winning the argument on whether they should be excluded from the total?

***Mr Hammond***: As I said, I cannot discuss a leaked document. However, we are having a discussion within Government about the appropriate way to record and then address net migration.

Q3 **Chair:** What is your view?

***Mr Hammond***: I am not prepared to discuss the contents of a leaked document.

Q4 **Chair:** Really we are no further forward. It would not surprise me that the overwhelming majority of the Committee agree with you on this issue. Indeed, I have got in front of me a quotation from Enoch Powell; even Enoch Powell agrees with you. In his "rivers of blood" speech, he made clear that international students coming to study here legitimately should not score as immigrants. We have got everybody onside here, backing you. I am hoping that you can give us some indication of the progress of your work.

***Mr Hammond***: This is a question of public perception and the public's view. Clearly, the level of net migration is an issue of concern to the public. The question we should be asking is: what does the public understand should be included within that definition? It is not whether politicians think one way or another; it is whether the public believe it. It would be very useful to explore that question.

Q5 **Chair:** We might come back to that question later on, but it would be extraordinary if that were to be the only issue that determines how we handle the 100,000 target and whether students should be included in it.

I would like to ask you a question about quantitative easing. The Prime Minister made an extended reference to this in her party conference speech. She concluded by saying, "A change has got to come, and we are going to deliver it". Looking carefully at the drafting of the speech, it is not clear whether or not that is a reference to monetary policy and QE. Was it?

***Mr Hammond***: My understanding of what the Prime Minister was trying to say is that we recognise monetary policy, which is an important tool of macroeconomic policy, has a distributional impact. To the extent that Government believe the distributional impact needs to be addressed or corrected, we also have tools available to us.

Q6 **Chair:** I am asking you whether the mention of "change" refers to a change in monetary policy or a change in fiscal policy.

***Mr Hammond***: It is a reference to the overall outcome, recognising that monetary policy is the responsibility of the Monetary Policy Committee, which is independent. We have no plans to change the way monetary policy is delivered or managed in this country. Fiscal policy has the ability, should the Government choose, to correct any of the distributional outcomes of monetary policy.

Q7 **Chair:** This was understood by the markets, as indeed it is still being understood right now, to mean that there will be a change in monetary policy. I take it those people are mistaken.

***Mr Hammond***: There will be no change in monetary policy. Monetary policy is independently determined. That will continue to be the case. The Monetary Policy Committee will continue to make decisions on interest rates and recommendations on unconventional monetary policy.

Q8 **Chair:** When you began your very first answer to this section on QE, you referred to your understanding, or words to that effect, of what the Prime Minister meant. Did you see this text before it was delivered?

***Mr Hammond***: I am not going to comment on the internal arrangements we have for co-ordinating and clearing speeches before party conferences.

Q9 **Chair:** Let me tell you what they have been every year that I have been involved in this process, which has been, on and off, for 30 years. They are always cleared. Even Gordon Brown used to let Tony Blair know roughly what was in his speeches. That is quite an impressive marker for relationships. Let me have another go: did you see the speech?

***Mr Hammond***: As I said, I am not going to comment on the internal processes of what was a party event, not a Government event.

Q10 **Chair:** That is, if I may say so, blisteringly clear in its lack of clarity. We will move on to a third issue; I am introducing a number of issues that others might want to raise. The Government are trying to work out what position they should take on Brexit. It has set up a Department to negotiate trade deals. That Department is now sending people all around the world, including Ministers, to discuss the possibility of new trade deals. Are we leaving the customs union?

***Mr Hammond***: The Government, as you said, are reviewing, gathering evidence and considering arguments around the appropriate negotiating stance for the forthcoming negotiations with the European Union, both on leaving the Union and on our future relationship with the Union. We have not made any conclusion yet as to the precise arrangements that we would seek. However, we are clear that this will be a negotiation between two sovereign entities—the United Kingdom and the European Union—and that we should not feel constrained by existing structures and arrangements. We should be able to talk about the way in which it would be mutually beneficial to construct future collaborative arrangements between the European Union and the United Kingdom.

Q11 **Chair:** In that case, we must be leaving the customs union, must we not?

***Mr Hammond***: We have not made any decision on that yet.

Q12 **Chair:** Can you explain how one can stay in the customs union and maintain this independent negotiation between two sovereign states, bearing in mind that within the customs union, trade policy is agreed collectively and is negotiated by the collective entity?

***Mr Hammond*:** The negotiation will be between the United Kingdom, on the basis that as we leave the European Union we will be a sovereign, independent state making our own decisions, and the European Union. Of course, we can use that sovereignty to agree an arrangement with the European Union if we believe that it is in our interest, and the European Union would presumably agree such an arrangement if it believed it was in its interest.

Q13 **Chair:** Again, we are not really making very much progress. We have got people going around the world negotiating, or trying to do the preliminary stages of negotiations, on independent trade deals. Unless you can be clear that we are leaving the customs union, that may be a complete waste of time. Do you think that it would be a good idea if the Government made up their mind, at least about this issue of staying in the customs union?

***Mr Hammond*:** I do not accept the premise of the argument. You have said that the trips made by DIT officials and Ministers would be a waste of time. I have heard it suggested elsewhere that DIT would not have a role. In fact, many European Union countries have trade ministries even though they are inside the customs union.

Q14 **Chair:** We are talking about the negotiations of trade treaties here.

***Mr Hammond*:** When DIT Ministers visit third countries, they are promoting British trade. Of course, in appropriate cases, they will also be exploring the openness of their interlocutors to potential negotiations.

Q15 **Chair:** Which trade deals has Germany independently done as a sovereign country?

***Mr Hammond*:** I did not say Germany had done any trade deals—

Q16 **Chair:** What about France or Britain? Those are the three largest trading countries.

***Mr Hammond*:** The role of a trade ministry is not limited to doing trade deals. It is also to promote and support trade. You will know very well that DIT has taken over the functions of UKTI.

Q17 **Chair:** Am I to take it that these people who are flying around the world are not in fact doing preliminary negotiations on trade deals, and that they are just doing trade promotion?

***Mr Hammond*:** In some cases they will be exploring the—

**Chair:** If the explanation you have given me is correct, they will be doing that in all cases.

***Mr Hammond*:** They will be exploring the appetite of their interlocutors for potential future trade deals with the United Kingdom. We are very clear that we are not able to enter into negotiations with third parties at the present time because of the constraints of our membership of the European Union. Certainly until such time as the Article 50 notice has been served, it would not be appropriate to enter into any substantive negotiation with any third party.

Q18 **Chair:** It takes years to negotiate these trade deals. Very few of them are done in short order. The sooner we get this under way and get clarity on this, the better for British interests, do you not think? Is this not the very uncertainty that is going to cost this country something?

***Mr Hammond***: It has become the convention to believe that it takes years to negotiate trade deals, and there have certainly been some very long, drawn-out multilateral trade deals. There is a reasonable argument advanced by my colleague, the Secretary of State for International Trade, that negotiating a straightforward bilateral trade deal ought to be a great deal simpler than negotiating a trade deal between a third country and a bloc of 28 countries.

Q19 **Rachel Reeves:** Thank you very much, Chairman. Thank you very much, Chancellor, for coming along to our Select Committee today. In April, the Treasury published an analysis on the long-term economic impact of EU membership and the alternatives. It says in that document that "the UK would be permanently poorer if it left the EU and adopted any" of these models"—the models that were looked at in that document. This was an official Government document at the time. Is it the Treasury's and Government's view that people are going to be poorer because of our decision in June?

***Mr Hammond***: The analysis that the Treasury published in April was based on a specific set of assumptions. It looked at three potential outcomes or stylised scenarios. At the time the analysis was done, those were the three alternatives to membership of the European Union that were current in the political discourse. It modelled outcomes based on the middle option of those three, and it did so, as all economic modelling inevitably does, against a set of assumptions.

Some of those assumptions have already proved to be invalid. One of them, for example, was that the Article 50 notice would be served immediately following a referendum decision to leave the European Union. That was a reasonable assumption, because that was the Government's policy at the time, but it has not proved to be the case. A second assumption, which is the kind that modellers tend to make, was that there would be no discretionary policy response to a decision to leave the European Union. However, the Bank of England, on 3 August, made a substantial monetary response. The validity of that model has therefore been challenged in at least two ways, in terms of assumptions that have not been met.

Q20 **Rachel Reeves:** Both of those things are correct, Chancellor, but the document I am referring to is about the long-term economic impact of EU membership, so I would have thought it was irrelevant whether Article 50 would be triggered immediately or at a later date. Similarly, the short-term response of the Bank of England in terms of interest rates, quantitative easing and other measures would not be relevant to the long-term economic impact, which is what the document I am referring to is about. I will give you another opportunity to expand on whether it is the Treasury's and Government's view that you stand by those long-term economic impacts, and whether the UK is going to be poorer. Is there a set of arrangements that would not see us poorer? You said that these were three stylised scenarios. Are any of those scenarios going to make us richer or as well-off as we are today?

***Mr Hammond*:** The longer-term model was also based on existing alternative models, but it is fair to say that it did not take into account some of the mitigations that we would expect to be delivered. For example, it assumed that existing EU trade arrangements with third countries would be replicated by the United Kingdom post-Brexit. However, it did not assume that we would enter into any additional free trade agreements with third countries.

It is clear that our objective is to enter into free trade agreements with our 10 principal trading partners. The Prime Minister has also been very clear that we do not accept that there are only fixed models that we can apply for. This will be a bespoke negotiation with the European Union around a potential bespoke solution, and therefore the model does not capture all of the potential outcomes.

Q21 **Rachel Reeves:** Does this document remain the Government position, as it was in April? Do you as the Chancellor stand by this Treasury document, or is it now redundant?

***Mr Hammond*:** It was the Government's position at a point in time, based on a set of assumptions, looking at three particular modelled outcomes. The Government's position now is that we will not be seeking to pursue any of those modelled outcomes. We will be seeking to pursue a bespoke outcome in this set of negotiations. We have already taken actions collectively; the Bank of England has already taken actions to mitigate the impact and short-term response. The point of this exercise is for us now to understand the challenges ahead. We want to make sure that we are able to manage and thus mitigate them, in order to get the best possible outcome and to create the opportunity to reach the benefits that are also out there. We have to be clear about the challenges as well as the opportunities ahead.

Q22 **Rachel Reeves:** To enable the Treasury and Government to make those decisions ahead of negotiations on our new relationship with the European Union, I assume that the Treasury is doing work, looking at scenarios above and beyond the three looked at in this document. Will you be publishing those scenarios so that we can have a public debate and some knowledge about the economic impact of the different scenarios we may enter into?

***Mr Hammond*:** As the Prime Minister has made clear, we will not be giving a running commentary. Exploring different options within negotiations is a substantial piece of work going on across Government, and of course we will be looking at the expected economic and fiscal consequences of different courses of action.

Q23 **Rachel Reeves:** Ahead of triggering Article 50, will the Treasury be publishing some analysis of what they think would be the impact of the negotiating position we are taking?

***Mr Hammond*:** There will not be one negotiating position. Anyone who goes into a negotiation with a single, fixed negotiation position is probably not going to get very far. It is important that the Prime Minister goes into these negotiations with a well thought-through range of options, understanding the costs and benefits of each and keeping them as closely held as possible. Publishing modelled outputs from different potential options is not going to benefit the UK in trying to get the very best possible deal as we leave the European Union.

Q24 **Rachel Reeves:** In your response to the Chairman's earlier question about whether students should be included in the target for net migration, you said that it was not for the Government to decide, and that we should consult the public to find out what they think.

***Mr Hammond*:** No, I did not say that at all.

Q25 **Rachel Reeves:** To have an informed economic debate about our future trade relationship with the European Union, it would be very useful for the public to see the costs and benefits of different arrangements, as the Treasury provided in the document in April. Can I ask again: will the Treasury be doing an analysis looking at the costs and benefits of different relationships with the European Union, and, if they do that work, will it be published so that the public can consider the costs and benefits of those different scenarios?

***Mr Hammond*:** To be clear and for the record, in responding to the question on migration, I did not say that it is not for the Government to decide. I did say that it would be useful to understand what the public thinks about an issue that is obviously of public concern.

I have been clear about the second part of your question. It would not be sensible, however irritating I understand it is going to be to some people, to go into a negotiation with all of our potential negotiating positions and all of the building blocks of a negotiating position spelled out in public, and with the costs, benefits and consequences displayed for our interlocutors on the other side of the table. I can promise you that the European Union will not be arriving at the negotiations with all the upsides and downsides of different negotiating positions set out for us to see.

We have to be clear here about our central purpose. We are leaving the European Union; we are introducing migration control between the European Union and the United Kingdom; and we are seeking, within those parameters, to get the very best deal that we can, so that British businesses and workers can sell their goods and services into the European Union. To do that, we need to maintain confidentiality around our negotiating stance. That is why the Prime Minister has said that we cannot give a running commentary on this process.

Q26 **Rachel Reeves:** To be able to make a decision about where you want to go as a British Government in these negotiations, the Treasury will have to do this work so that you can go to the Prime Minister and say, "This is my considered opinion of the different options, and this is where I think we should go." You will be doing that work internally in the Treasury.

***Mr Hammond*:** Of course we will be looking internally at the various different options and what the costs and benefits of them are.

Q27 **Rachel Reeves:** But that information will not be available either to this Committee, the House of Lords Committee, parliamentarians or the public to be able to debate, scrutinise or consider the alternatives. That will not be available to us.

***Mr Hammond*:** We cannot have a public debate about what our negotiating position is going to be. If we were to do that, we would have no negotiating position.

Q28 **Rachel Reeves:** We will not be having a public debate, Chancellor, about our future relationship with the European Union. We must now leave that in the hands of the Government?

***Mr Hammond*:** That is a ridiculous extrapolation, if I may so. Of course we will be having a public debate. Clearly, we are having it every single day; you only have to open a newspaper. However, we cannot publish the various options that Ministers will be considering and the modelled outputs of those options in terms of costs and benefits. That would be to undermine our negotiating position in a spectacular way.

Q29 **Rachel Reeves:** A public debate is very difficult to have, Chancellor, without the evidence being made available, either to parliamentarians or the public. We can have a public debate, but it will not be with the facts available to us. That will be a very poor public debate, and it is a very disappointing decision by the Government.

***Mr Hammond*:** I would suggest to you that there will be plenty of people producing material, including modelling, between now and next March.

**Rachel Reeves:** Taxpayers pay for the Treasury to do that work, Chancellor. The public and parliamentarians deserve to see that work.

Q30 **Chair:** I have to say that I expect that is a majority view around this table. The heart of the matter, though, is that we are having a public debate. The public debate occurs every time the Brexit Cabinet sub-committee meets; within 24 hours, we have a very full and public debate. I am not going to tire everyone in the room with the long list of leaks there have been, but we can identify the dates of meetings, even if they are not made public, merely by the arrival of the newspaper articles.

Do you not think that publishing proposals would be a far more intelligent way to have a debate, rather than carrying on with the idea that we cannot say anything because it will interfere with our negotiating position? We are having a running commentary anyway. The Government cannot keep matters secret for 24 hours. Once it gets into the hands of our counterparties—27 countries and the EU—it might as well be published in the newspapers.

***Mr Hammond*:** It would be far more helpful to this debate if we were able to conduct these internal discussions privately without leaks to newspapers. We need space to explore different options and to discuss among ourselves. It is no secret that there are different views about how we should approach the negotiation, and we are exploring together how to give the Prime Minister the very best negotiating hand.

Q31 **Chair:** Your first sentence gives a pretty clear view of your own attitude. Whether or not one agrees with it is another matter. You have also said in response to Rachel Reeves that it is clear that your objective is to enter into free trade agreements. We are back to our old friend the customs union, are we not? You cannot do an independent trade deal from within a customs union, can you, Chancellor?

***Mr Hammond*:** I was talking there about the long-term model. If we were to have a long-term outcome that involved not having substantial access to the markets of the European Union, we would clearly be looking to expand our markets in other areas through free trade agreements.

Q32 **Chair:** You also said that we ought to find out what the public think about whether or not students should score as immigrants. Of course, we have extensive polling evidence on just that, and I have got some in front of me now. It shows that only a fifth of people think that international students count as immigrants. Do you think that we need to do a good deal more polling evidence, or do you think that we can rely on the information in the public domain?

***Mr Hammond*:** That is very interesting information and I am sure it will be noted.

Q33 **Chair:** Are you aware that 59% of people are opposed to any efforts to reduce the number of international students in the UK?

***Mr Hammond*:** I have not seen that polling output, but it is very interesting.

Q34 **Wes Streeting:** I agree with my colleagues about how unfortunate it is that we are not going to have more information in the public domain. We are not asking for the negotiating position; we are asking information that will inform the public as to judge how good a job you have done. That is perhaps why the Government are not keen to have that information in the public domain.

I will begin with an area of what I hope will be consensus. A majority of people have voted to leave the European Union. We are leaving the

European Union, and it is fair to say that the majority of parliamentarians, like you and I, who were remainers, accept the result and are now committed to making the best of it. Do we agree on that?

***Mr Hammond*:** We can agree.

Q35 **Wes Streeting:** We are in absolute agreement. In terms of both maximising the opportunities and mitigating against the risks, there are a range of options that we can pursue, as you have said, as part of the negotiations. When you are putting forward options that would mitigate against the economic risks, you must feel frustrated to be portrayed through briefing to the media as a saboteur of the Brexit process. Is that fair?

***Mr Hammond*:** The best way to support this Brexit process and make sure that we get the right Brexit for Britain is to give the Prime Minister the maximum space at the negotiating table, within the two clear constraints that we have made the irreversible decision to leave the European Union and that we are going to control migration between the European Union and the United Kingdom. Beyond that, she needs the maximum possible space.

My objective in supporting the Prime Minister is to make sure that she has the broadest range of options, properly costed and understood, and the maximum scope to deploy that broad range of options in what might be a wide-ranging negotiation across a very broad spectrum of areas. Those that are undermining the effort are those that are seeking to close down that negotiating space, seeking to arrive at hard decisions that we do not need to make at this stage. Keeping as many options open as possible is the key to the strongest possible negotiating hand.

Q36 **Wes Streeting:** I agree with you. Could you tell us a bit about your role in the process and whether you will be at the negotiating table with the Prime Minister, as part of the team? I was concerned listening to the speeches at Conservative party conference. What actually concerned me more than the issue that dominated the headlines, which was treatment of migrants, was mostly the Prime Minister's speech on the Sunday, where she said, "Let's get behind the team of Ministers—David Davis, Liam Fox, Priti Patel and Boris Johnson—who are working on our plan for Brexit, who know we are going to make a success of it and who will make a reality of global Britain." Are you not working on our plan for Brexit and why were you omitted from that key team?

***Mr Hammond*:** I am indeed, as are several other Ministers that were not in that list of names. We have a small Cabinet committee dedicated to this issue, as you know, but, as you would expect, it is a major topic of bilateral discussion between me and the Prime Minister.

Q37 **Wes Streeting:** The reason I am concerned, and this brings me to the line of questioning I have about our relationship with the single market, is that the key tension here is that, in order to deal with the issues around freedom of movement and immigration, which were at the centre of the debate, there are inevitably some compromises and trade-offs. You have talked about those, but they also pose risks in terms of our economic voice. I am concerned that the voice of the Treasury and the voice of the Chancellor may not be at the heart of the process, but you are giving us the reassurance that you are part of the process.

***Mr Hammond*:** I can reassure you that it is.

Q38 **Wes Streeting:** On 14 July, the day after you became the Chancellor, you said, "We will come out of the single market as a result of our decision to leave the European Union". Was that Government policy or a personal view?

***Mr Hammond*:** The key thing here is that we have spent a lot of time around whether we are in or out; do we have access? This is accepting the status quo as the starting point. We believe that we have reset the status quo. By voting to leave the European Union, by voting to become a full sovereign nation again, we are able to sit at this table and start from scratch, to say to our partners, "What is the best way to design a relationship between the European Union and the UK that works for both parties?" We should not be hung up about customs unions and single markets. Let us talk about the substance, not the format.

Q39 **Wes Streeting:** With respect, Chancellor, I have just raised a very substantial point, which is about membership of the single market, repeating back to you a view you expressed the day after you became Chancellor. I absolutely agree, so let us go right to the substance. Was that Government policy or a personal view? It sounds to me that, as a result of discussion with colleagues and sticking to the open-minded approach you have adopted, that is no longer your view. Is that fair? Are you more flexible now than you were?

***Mr Hammond*:** I do not think that the language we use is the key issue. The key issue is whether we have free access to our goods and services, for our companies to operate in and trade with the European single market. Now, there are different ways of describing that relationship. A lot of energy has been expended trying to create the different ways of describing it.

Q40 **Wes Streeting:** I do not think I am being particularly flowery and descriptive in my language. I am talking very specifically about membership of the single market. These are specifics, not a load of flimflam. I am asking very specifically about membership of the single market.

***Mr Hammond*:** The important thing is that we have access for our companies and our businesses to sell their goods and services into the single market and to operate inside the single market.

Q41 **Wes Streeting:** That sounds a lot less precise than what you said the day after you became Chancellor. Let me then try to get you on to some of the trade-offs. In an article you wrote back on 4 July, while you were

Foreign Secretary—things may have changed considerably if they have changed since you became Chancellor—you talked about the central trade-off between access to the single market versus freedom of movement: "Those who believe there is no need for such a trade-off have misunderstood…the politics of the European Union." You added, "There is a range of outcomes between 'no access' and 'full unfettered access' to the market; and…a range of…restrictions on free movement…So rather than squandering…time and negotiating capital…let's recognise" the trade-off "up front and scope the options…within the boundaries." Is that still your view as Chancellor, now you have moved on?

***Mr Hammond*:** In fact, I said the very day after the referendum that clearly the central trade-off would be around the European Union's negotiating position. It is their clearly stated negotiating position that access for goods and services to the market is linked inextricably, in the view of their opening position, to freedom of movement. Now, we can choose to ignore that. We can seek to move them away from it, but the fact is that the European Union has been pretty clear and pretty consistent in setting that out as their opening stance.

Q42 **Wes Streeting:** One of the things that follows on from that answer is where we might find ourselves in between. You said shortly after the referendum that "leave" campaigners have to make those trade-offs between the different things that they were promised and those that were mutually incompatible. I wonder if you have a view or worry about what "leave" voters will be most disappointed about, as a result of this process. Will they, for example, be disappointed by the absence of a substantial fiscal dividend from Brexit?

***Mr Hammond*:** That is probably for others to answer. I did not propose to anyone that there would be a substantial fiscal dividend, but I did make it clear in my conference speech, which you clearly will have read, that whatever the history, whatever side of the argument we were on, we now have to understand how we were mandated on 23 June. I take it as a given that, in mandating us to leave the European Union and mandating us to control migration between the EU and the UK, the British people would expect us to do that in the way that best protects their jobs, their prosperity and their future.

Q43 **Wes Streeting:** You made a fair initial point, but the rest of my questions are probably better directed at David Davis and we are hoping to see him soon. I know that Stephen Hammond is going to come on to talk about financial services in particular, but you cannot have escaped the very clear message that is coming from our financial services industry. They are incredibly concerned about issues and the lack of clarity and certainty around access to the single market, membership of the customs union and the whole range of other factors that exist. Without that clarity, many of those companies are saying that they are going to have to start thinking about activating their contingency plans sooner rather than later—that is, when we trigger Article 50—because some of these contingency plans will take two years. Given that instability and uncertainty, and the risk, have you got the message and will you make sure that, at the top of our list of demands, is a clear, sensible period of transitional agreements, so that people can prepare the transition from the status quo we have now to whatever the outcome of the negotiating process is?

***Mr Hammond*:** You are quite right to identify the fact that uncertainty is the big challenge in the next phase of this process. It is a challenge to our economy that there will inevitably be a period of uncertainty, until we know the outcome of the negotiations. There will then follow a different period of structural adjustment, where we have certainty and we have to change the way our economy works to respond to that certainty.

I have had many interactions with financial services companies here, in the United States and across Europe. You are absolutely right to say that one of the mitigations that the industry is proposing is some kind of transitional period that gives them longer to adjust to whatever the outcome of the negotiations is. We understand that ask from the financial services industry but, as the Prime Minister has said many times, we are not going to give a running commentary on how we will conduct the negotiation and what our priorities will be within it. To do so would be to give away negotiating advantage, but of course it has been noted.

**Chair:** It has been pointed out that of course we are having a running commentary. It appears every time the Brexit committee meets. Perhaps the best way to prevent a running commentary is for the Brexit committee not to meet.

Q44 **Helen Goodman:** Good afternoon, Chancellor. You say that it is not a good idea to take early decisions and that it is important to do some thinking about all the possibilities. That is extremely sensible. One of the things I am concerned about is the impact on the UK economy if we leave the customs union. It is clear that the other EU member states would expect British exporters exporting into the union to comply with the rules of origin, and the OECD has estimated that this adds 24% to the cost of goods. This was in the Treasury's analysis that was published before the referendum and, on the front page of *The Guardian* today, there is a story saying that the Treasury has concluded that leaving the customs union would cut GDP by 4.5%. Are you doing work on the impact of leaving the customs union?

***Mr Hammond*:** I cannot comment on a leaked document.

**Helen Goodman:** Of course you cannot. I am not asking you to.

***Mr Hammond*:** Clearly the *Guardian* article was reporting a discussion that it claims was held in the same committee last week, which answers your question. Yes, clearly work is being done on this issue by the Department for Exiting the EU and the Treasury, working together in collaboration.

Q45 **Helen Goodman:** Chancellor, I want to assure you that we are from the Treasury Committee and we are here to help you. In Norway, the rules of origin are found to be so onerous that some people have decided that it is cheaper to pay the tariff than to go through the bureaucratic process. Have you made an assessment of the loss of competitiveness if UK exports into the EU had to pay the tariffs?

***Mr Hammond*:** Helen, certainly one of the areas that we are studying is what the implication of WTO tariff regimes would be for different sectors of the UK economy. It obviously bites differently on different sectors, because tariffs vary enormously under the WTO rules, just as we are looking at the different components of the customs union. The customs union is about country-of-origin rules; it is also about processes and procedures at borders, physical controls, and the inefficiencies that they can introduce into logistics processes.

I can assure the Committee that the Treasury, working with other Departments of Government, is looking at all of these areas and many more to analyse the benefits and the costs of different courses of actions, so that the Prime Minister can be fully informed when she has to make difficult decisions, trading off between different possible solutions in a negotiating process.

Q46 **Helen Goodman:** Obviously there is no point in just saying it will just be like Norway, because Britain has quite a different economy from Norway. I am pleased to hear that you are you looking at different sectors. Are you looking in particular at those industries like pharmaceuticals, automotive and aerospace, with complex integrated supply chains, where this aspect of the rules of origin will be particularly burdensome? Have you included them?

***Mr Hammond*:** Of course. We are looking at all key sectors. You are right that we should take particular note of those sectors with complex pan-European supply chains, where components and sub-assemblies often move backwards and forwards several times, across European borders, before they are incorporated in a final product.

Q47 **Helen Goodman:** I am pleased to hear that, because I know you are subject to a lot of lobbying on financial services and I want to be reassured that you are taking account of the 3 million jobs in manufacturing in this country.

Can I turn to the impact on agriculture if we left the customs union? Obviously the processes would slow down the export of goods into the EU. Have you made any assessment of the potential loss of exports from the agricultural sector and perishable goods?

***Mr Hammond*:** I can only repeat that the Treasury is doing a lot of work with other Departments in Government, across all of these areas, and sectoral analysis on imports and exports for all the different key sectors.

Q48 **Helen Goodman:** Is that also by region? Could I suggest that the

Treasury does look at regions?

***Mr Hammond*:** I am pretty confident in saying that we are also doing some work on regions, but I cannot give a running commentary on every piece of work that we are doing.

Q49 **Helen Goodman:** I am not asking you to give a running commentary, Chancellor. Obviously as you have pointed out, there is a choice to be made between the loss to competitiveness from 44% of British exports that go into the EU if we were to leave the customs union, given the negotiating position of the EU, and the potential gain from better free-trade deals with third countries. Have you made any assessment as to how much the growth of trade to third countries would have to be to overcome potential loss of exports to the EU?

***Mr Hammond*:** We do not accept that it is a binary situation. There is a huge range of potential outcomes. It is not a single trade-off; there are many areas where we can negotiate potential outcomes within a range, with our EU neighbours. I am not going to be tempted into giving a list of all the different pieces of analysis that we are doing, still less the outcomes of those pieces of analysis. I can assure you that the Treasury, working with other Government Departments, is doing detailed work in all of the areas that you would expect it to be, in all of the areas where the big choices will be made.

Q50 **Helen Goodman:** Chancellor, I think the British Government's line on running commentary will come unstuck at the point at which Angela Merkel has to go to the German Parliament to display her negotiating hand. It will then be the case that many other European Parliaments know what their country's negotiating hands are. The only one that will not will be the British Parliament. Have you had any representations from the Irish about the difficulties that it will cause them if they have to introduce border checks in order to ensure that the British fulfil the rules of origin on exports into the Republic?

***Mr Hammond*:** Yes, of course. We have had lots of discussions with our Irish counterparts, because we are acutely conscious of the fact that the Irish Republic is, arguably, the country most affected by Brexit, apart from the United Kingdom, because of the unique geographical nature of the land border and because of Ireland's geographic position, effectively separated from the European Union by the United Kingdom. As you know, we have made a commitment that we will do everything in our power to ensure that, whatever the outcome, it does not involve a hard border between the UK and the Republic of Ireland, for all the obvious reasons.

Q51 **Helen Goodman:** The Chairman has given me three minutes, so I will just ask one short question. Would you put on your wide range of options to consider the possibility of not being a member of the single market, but staying in the customs union?

***Mr Hammond*:** As I said, I am trying not to rule anything out.

**Chair:** You are trying not to say anything at all, as far as I can tell.

***Mr Hammond*:** Every possible combination should be considered, because I genuinely believe that, every time we rule something out, we hand a negotiating chip to the opposite side of the table. Keeping as many things on the table as possible is the best way to negotiate.

**Chair:** We have heard that view.

Q52 **Mr Rees-Mogg:** Thank you, Chancellor. I am very encouraged by your answers. I think you have been maligned by the press, who have you down as a remainer, whereas I think everything you have said has been a very positive view of how Brexit can be made successful, so thank you very much. What I wanted to ask about was on the customs union issue. What are your views on free trade generally? Where do you stand philosophically on the free trade argument?

***Mr Hammond*:** First of all, on your first comment, my job is to make Brexit a success. My job is to look at the economy, the challenges it will face and the opportunities that will be in front of us, to make sure we are well equipped to seize those opportunities, but also to make sure that we spot the challenges coming, we prepare for them, we manage them and we mitigate them.

On the question of free trade, my view of the world is that free trade is a positive. It enhances competitiveness. It allows countries to focus on areas where they have comparative advantage and it allows all of us to be better off, but I am acutely aware of the fact that there is an increasing backlash in the world to trade. Trade deals are getting more difficult to negotiate. World trade is slowing alarmingly. The IMF estimates that, this year, world trade will grow at half the rate of world GDP growth whereas, traditionally, it has grown at twice the rate of world GDP growth. That should be truly alarming to us. I think it just sets the context: there are a lot of challenges facing us; not all of them are created by Brexit. Some of them are created by headwinds in the global economy.

Q53 **Mr Rees-Mogg:** You were very interesting in relation to the Treasury document on the long-term outlook for the economy in the event of Brexit, and the importance of underlying assumptions and how, if they change, conclusions change. It seems to me why you are right to keep your discussions confidential and the other assumptions that you make, because essentially, if they are in the public domain, they are used to advance an argument, rather than necessarily to provide independent analysis. In that document, it assumed that, if we were just on WTO terms, we might have to apply tariffs to the European Union's exports to us. As a free trader, do you ever think that would be realistic?

***Mr Hammond*:** It would entirely be our decision, of course. Clearly there would be a political pressure for reciprocity. There might be an economic argument against reciprocity. I absolutely recognise that fact, but this is not a decision that we have to make at this stage.

Q54 **Mr Rees-Mogg:** No, but as Chancellor could you foresee circumstances where you would stand up in Parliament and, in 19th-century terms, put a tax on bread?

***Mr Hammond*:** I am a free trader by instinct, Mr Rees-Mogg, but as we go into a negotiation with the European Parliament, setting out red lines that we would not transgress for ideological reasons would be very unwise indeed.

Q55 **Mr Rees-Mogg:** I see the sense in that but, very importantly, you also said that it would be our choice and that this would apply to any customs checks and controls we put on any goods coming into this country.

***Mr Hammond*:** That would be subject to the rules of any organisation of which we were a member, which of course includes the WTO.

Q56 **Mr Rees-Mogg:** Assuming we apply the same rules to everybody, which the WTO requires, stories about us needing to employ an extra 5,000 customs officers and so on, all of that would be our choice, rather than a necessary concomitant of leaving the customs union.

***Mr Hammond*:** It would be our choice, of course. Assuming that we wanted to operate an efficient at-the-border customs system under WTO rules, we may need significantly more infrastructure at the border than we have now.

Q57 **Mr Rees-Mogg:** We would not if we are genuinely in favour of free trade, because we can ease the passage of these goods very swiftly. You nodded.

***Mr Hammond*:** The logic of your argument is faultless.

**Mr Rees-Mogg:** Thank you very much. I was saying to Mr Streeting, before you appeared, that in previous sessions he agreed with your predecessor more than I did and I hoped it would be the reverse this time around. It seems we are getting to that happy state of affairs.

***Mr Hammond*:** I hope we will find that we are all in violent agreement that we are now trying to find the best way to have the best possible deal for Britain, as it exits the European Union.

**Wes Streeting:** I think you have overstated my agreement with the previous Chancellor as well. I would like that on the record. I have enough trouble as it is, thank you.

Q58 **Stephen Hammond:** Good afternoon, Chancellor. Thank you for appearing. Mr Streeting said I was going to ask you about financial services. As you know, financial services is 2 million jobs in the UK. It is the largest tax-paying sector. It is the largest export sector. It is the sector in which we enjoy the largest surplus, probably the only sector where we enjoy a large comparative surplus with the EU, and yet financial services as an industry feels that the Government are indifferent to its plight, in terms of these negotiations. *City A.M.* loudly trumpeted that again this morning. I wonder why you think financial services has this view. Do you think that, across Government, there is a recognition of the importance of this industry and its comparative advantage to this country?

***Mr Hammond***: Yes, I do. We are all acutely aware of the fact that, notwithstanding the rhetoric immediately after the financial crisis about rebalancing the UK economy, the reality is that financial services remains our single largest sector. It is responsible for a very large number of jobs spread across the United Kingdom. This is not a London-based industry, and it plays a very important role in our external current account balance, as you rightly say, providing one of the few bright spots in terms of the positive current balance with the rest of the European Union. The industry knows that we regard it as extremely important. The industry knows that we understand that it has a particular set of challenges, as we go into this period of negotiation with the European Union. I hope the industry knows—it certainly should know—that helping to address those challenges and take account of those challenges will be a very high priority for the Government.

Q59 **Stephen Hammond:** I think that is important to get on the record, because I think that industry thinks that, while you and the Treasury are of that view, it may not be a widespread view across the whole of Government. Indeed, one of your senior colleagues has downplayed the importance that the Government have attached to the retention of passporting for the success of the sector. Do the Government accept that passporting is key to the success of corporate banking in London?

***Mr Hammond***: Passporting is of course important. The retention of passporting would mean that the problem went away, as far as almost all financial services businesses were concerned. From the point of view of the financial services sector that would be the ideal outcome. In the discussions that I have had with the financial services sector—and I have spent a lot of time with financial services companies here, European financial services companies and US providers—they are also realistic and are looking at other options beyond passporting to protect their interests. We are obviously working closely with the industry on looking at all the options for future protection of London's financial services businesses.

Q60 **Stephen Hammond:** You have used that phrase again, Chancellor, "other options". I was going to quote the fact that, in response to Mr Streeting, you used the phrase "different options". While there are a range of options that may or may not be available, EEA membership and unilateral equivalence regimes are not going to be acceptable, either to the Government politically or to the industry, in terms of the risk they expose. It therefore implies that the Government have to be prepared to look at a hybrid model, which will accept access for limited movement of jobs within the industry and a bilateral equivalence regime. How achievable do you think that might be?

***Mr Hammond***: We would call it a bespoke model. I am on the record as saying to the House of Lords Committee that, as we move to introduce controls on migration between the European Union and the UK, and without prejudice to what system we eventually decide to adopt, I cannot conceive of any circumstances in which we would be using those controls to prevent banks and companies moving highly qualified, highly skilled people between different parts of their businesses. That is essential for the smooth operation of our economy. Going back to the discussion we had at the beginning of this meeting about public attitudes, when the public tells us loudly and clearly that they have a problem with levels of migration, it is very clear to me that they are not talking about computer programmers, brain surgeons, bankers and senior managers.

**Chair:** Or students perhaps.

***Mr Hammond*:** Possibly students; they are talking about people competing for entry-level jobs with people in the UK, who perhaps have a level of skills that means they only have access to those kinds of jobs. We need to reassure the financial services sector but also others, such as the tech sector, that in fact, if they look at our track record of how we manage migration from outside the EEA, we already have a regime that readily facilitates people coming from outside Europe to work in financial services businesses and other people with high skills coming to work in the UK. That is not where the problem lies and that should not be where the concern of business is.

Q61 **Stephen Hammond:** You very rightly call it bespoke. I think the first part of your answer gives some hope that that bespoke model might be possible. That is good news. Could you say whether or not the Treasury has done any work on the potential systemic risks if a transactional arrangement is not reached?

***Mr Hammond*:** This is less a role for the Treasury than for the regulators, but it is the case that regulators on both sides of the English Channel and indeed both sides of the Atlantic are starting to think about how any change in the structure of financial services markets in Europe takes place in a way that does not have any negative impact on financial stability, either domestically or globally.

Q62 **Stephen Hammond:** Would you recognise that one of the major US investment banks and others that I have spoken to are saying that the regulators are already putting pressure on them to come forward with arrangements for transition in case of that systemic risk? They are being pressurised to do so within the next six to nine months. Therefore, unless there is some framework in place to reassure them, we risk losing those businesses from London or from the UK.

***Mr Hammond*:** If I may say so, that is a different question. We are in a negotiation with the European Union and there will be negotiating positions taken up. The French have been circulating prospectuses to financial services businesses, suggesting reasons why they might wish to relocate to Paris, so there is a certain amount of competiveness in this. Where we have a shared interest, and it goes well beyond the UK and the

European Union, is in avoiding any risk to financial stability. We all remember only too well, from 2008-09, what happens if financial stability is challenged. All parties will want to work together to make sure that what is done is done in a way that supports and underpins financial stability, not challenges it.

Q63 **Stephen Hammond:** On our recent visit to the continent, the Treasury Secretary took some evidence from regulators. There was some concern from regulators about their competence to accept businesses moving out of London to other locations in Europe. Is not the major threat to London not from other centres in Europe, but potentially from Singapore, Tokyo and New York?

***Mr Hammond*:** There is certainly a stream of thought from financial services businesses, particularly US-based ones, that it would be wrong for anybody to assume that if they were not able to conduct business in London, they would conduct it from somewhere else in Europe.

The financial services market in London, because of its depth and breadth, is highly efficient. That means that quite a lot of quite marginally profitable activity can be sustained because of the scale of operations in London. If those operations were forced to be fragmented, the economics of providing some services would change radically. The temptation either to stop providing some services or to repatriate them—in the case of American businesses, to repatriate them to New York—would be quite strong, I suspect.

Q64 **Stephen Hammond:** Finally, Chancellor, as you know financial services hang on the every word of a Chancellor twice a year, at the time of the Autumn Statement and at the time of the Budget. I note your desire not to pull rabbits out of hats. I wonder if you are considering whether or not two statements is one too many.

***Mr Hammond*:** I am aware of the views of the Institute for Government, the Institute for Fiscal Studies and others on this subject and will look carefully at their representations, along with every other representation I receive ahead of the Autumn Statement.

Q65 **Chair:** Would you like to give that reply to my next question as well? I think it is a very reasonable reply, bearing in mind the request. I just want to clarify one point that Stephen made there. Are you clear that falling back on equivalence without the support of a bespoke arrangement would be damaging to the UK financial services industry?

***Mr Hammond*:** Equivalence is one of the routes being discussed by players in the financial services sector, but of course it has some challenges around it, not least that the decision on granting equivalence and continuing equivalence would lie unilaterally with the Commission.

**Chair:** It could be withdrawn at any time.

***Mr Hammond***: It would not be a stable basis on which to plan long-term.

Q66 **Chair:** So the answer is yes, it would not be a stable basis on which to plan long term.

***Mr Hammond***: In the absence of an agreement.

Q67 **Chair:** When you say an agreement, you mean a bespoke deal or something to support it. I am only using your terms in response to Stephen's question.

***Mr Hammond***: Clearly conceptually, an agreement around the way equivalence was granted and maintained could change the dynamics of an equivalence regime and the extent to which financial services businesses could rely on it.

Q68 **Chair:** Are you clear, as many in the City are, that passporting is a goner?

***Mr Hammond***: No, I do not think we should take anything off the table. We should not concede anything at this stage of the process. We are very much aware that that would be the financial services sector's first preference, but we are also acutely aware of the challenges of delivering it.

**Chair:** You are aware of the difficulties of that, too. That is a very, very helpful clarification.

**John Mann:** Welcome, Chancellor. After an hour of saying absolutely nothing, you have suddenly opened up. I hope it is going to continue.

**Chair:** He has certainly said something now.

Q69 **John Mann:** We know about free movement for bankers, computer programmers, brain surgeons and students, but the possibility of a restriction on entry-level jobs. Farmers have to bring in, so they say, large numbers of unskilled workers to pick fruit and vegetables. What certainty do farmers have that they will be able to bring in the same type of labour, as they have been bringing in?

***Mr Hammond***: Just to be clear for the record, I did not talk about free movement. I talked about us using whatever migration control regime we decide to put in place in a responsible way, which would support the economy. What I said was that I cannot conceive that that would involve us preventing companies from bringing in high-level employees, highly paid, highly skilled employees, to work in their businesses, which are supporting the British economy. That is not free movement as the Europeans would understand it, because the Europeans understand the term "free movement" to mean free movement as of right for every citizen of the European Union. That is not what we are proposing and not what would be acceptable.

You ask about the challenges facing the agricultural sector. Again, they are a different set of challenges, which historically have been dealt with differently in our immigration system. I have no doubt that we will be able to look at an appropriate way of addressing the needs of the agricultural sector in a migration control regime between the UK and Europe.

Q70 **John Mann:** That is useful clarification. Mr Bowman, you have to produce all the figures, or your people do. As you know, the Government's long-term economic plan is predicated on a net migration into the labour force of 200,000 a year up to 2020. Have you changed that?

***Mark Bowman*****:** It is the OBR that will produce the forecast and the OBR traditionally uses the ONS projections for migration.

**John Mann:** The OBR forecasts, but you provide the tax revenues and spending plans based on that. You and I have had these debates before. It is predicated on 200,000 net new migrants into the labour force, every year up to 2020. Have your projections for that changed?

***Mark Bowman*****:** We do not make projections. It is the OBR that does the economic forecast. It bases its migration assumption on the ONS numbers. It is not an input from the Treasury; we do not tell the OBR which migration numbers to use. It is their economic forecast and they use the ONS numbers.

**John Mann:** I will take it that there is no change in your approach then.

***Mark Bowman*****:** It is a question for the OBR.

Q71 **John Mann:** I am checking in terms of the work that you do. I am going to ask the OBR, but I asked you. I presume from that that there is no change to your approach, in your Department. On law-abiding EU citizens working in this country, Chancellor, are there any scenarios in which you could see any of them being deported in the next five years?

***Mr Hammond*****:** We very much hope that we will be able to reach an agreement with the European Union that assures reciprocal rights for EU citizens in the UK and UK citizens in the EU who are already established. We hope and expect that that will be possible. There have been few, if any, voices raised against such a resolution of this particular question.

Q72 **John Mann:** There is a scenario where you could see deportation then. That is also useful to clarify.

***Mr Hammond*****:** I am not quite sure how you have reached that conclusion.

**John Mann:** If you do not reach agreement, there is a scenario there.

***Mr Hammond*****:** I would expect that we do reach agreement.

**John Mann:** But it is predicated on reaching agreement.

***Mr Hammond*:** Of course there has to be an agreement.

**John Mann:** It does not have to be predicated on that. It is a choice. That is what I was clarifying. You have clarified that.

***Mr Hammond*:** No, I have not. You are extrapolating too far. I have said that we would hope and expect to reach an agreement that reciprocally assures the rights of EU nationals in the UK and UK nationals in the EU. If we fail to reach such an agreement then, under a migration control regime that was unilateral, that was a UK regime, we would have choices to make about how we chose to deal with those EU nationals in the UK. It would be a matter for the UK to decide.

Q73 **John Mann:** There is a scenario, then. Some people, including myself, would think there is quite an opportunity to do what the French and Americans tend to do, which is to buy British. Buy British on major defence contracts. Buy British on major infrastructure. Do not get hung up, like your predecessor did, on competition as a requirement, as you did as Defence Secretary.

***Mr Hammond*:** It was as Transport Secretary.

**John Mann:** In terms of industrial strategy in this new era, do you anticipate that there will be and needs to be a "buy British" strategy, particularly for manufacturing, defence and major infrastructure projects?

***Mr Hammond*:** I would expect that we will want to introduce our own bespoke competition policy and procurement policy, which will seek to encourage the UK supply chain, but will certainly not want to create the situation where UK Government procurement is buying uncompetitively expensive products. That would not be in our interest.

Q74 **John Mann:** We have a disagreement. I am sure that we will be able to go through that disagreement in the next year or so. Your close former colleague, friend and political ally William Hague has stepped into the argument very strongly in attacking the independence of the Bank of England. Some people would think that that is part of a concerted approach, for whatever reason—let me not speculate why—on attacking the independence of the Bank of England. Can I give you the opportunity to slap him down?

***Mr Hammond*:** You have certainly given me the opportunity to suggest that you may know nothing about my relationship with William Hague, former party leader, who I was very privileged to work with, but I would hardly describe him as a close friend. I have not had any contact with him at all since he left the House of Commons. I have made the Government's position on the Bank of England clear. The Bank of England will remain; the Monetary Policy Committee will remain responsible for the independent formulation of monetary policy, as it is now. There are no proposed changes to that regime.

Q75 **John Mann:** The whispers coming from Government in relation to that should, then, be ignored by us, by the City and indeed obviously by the Bank.

***Mr Hammond*:** I do not know how you define "whispers". The Chairman, I think it was, read out part of the Prime Minister's speech to the party conference. That can scarcely be described as a whisper, since it was delivered to a television audience of millions. I have already explained how we see this: monetary policy is independently determined. It is an important part of macroeconomic policy. It has certain distributional consequences and the Government has the tools available, where it feels the need, to address those distributional consequences through the way it operates fiscal policy.

Q76 **John Mann:** I hope you will be taking on Mr Hague rather directly then, in the things that he is suggesting. It would be helpful if you did. My final question then is on your predecessor's powerful advocacy, including regularly at this Committee, for devolution, not least to the north, for city regions and elected mayors. He was a key dynamic behind that. There are many decisions on that, imminent or not imminent, depending on the Government. Do you have the same drive behind that or are you veering in a different direction?

***Mr Hammond*:** I support the Northern Powerhouse project. I was a strong backer of it from its inception. I absolutely agree with the Prime Minister that we need to unleash the power of our cities across the country, not only in the north, but this is at the heart of our productivity agenda. If you look at the UK's poor productivity performance and seek to analyse its roots, one of the things that immediately leaps off the page is the gap between the productivity performance of London and the productivity performance of our second, third and fourth cities. That gap is without parallel anywhere else in the developed world. Raising the productivity performance of those cities and better still city clusters, in the north, the midlands and elsewhere in the UK, is one of the keys to addressing the productivity challenge that we face in this country.

Q77 **John Mann:** I am very confident that if George Osborne was sat in that seat today, he would be saying to those Labour and Tory councillors with deals for city regions and mayors in front of them to get on board and sign them. Would you give the same message today?

***Mr Hammond*:** Yes, indeed. It is happening. People are getting on board and signing deals. We are negotiating further deals. This whole project is making substantial progress and we will continue to drive it.

Q78 **Chair:** Chancellor, in response to an earlier question from John Mann, you seemed to come close to ruling out deportation of existing EU nationals. Did you?

***Mr Hammond*:** It is a deliberately emotive word. What I said, very clearly, was that we hope to reach a reciprocal agreement that protects the interests of EU nationals in the UK and UK nationals in Europe.

Q79 **Chair:** I am just trying to clarify whether people who are already here could be confident that they will be able to remain.

***Mr Hammond*:** If we do not, it will be for this Government to decide how we treat those people.

Q80 **Chair:** Yes, but we could take that decision now, could we not, Chancellor?

***Mr Hammond*:** Of course we could.

Q81 **Chair:** I am just asking you whether we, as a Government, are thinking carefully about that question, to the point where we will be able to stay, "They're going to be able to stay here."

***Mr Hammond*:** In my previous role, I answered a very similar question before the Foreign Affairs Committee, shortly after the referendum. We have a significant number of British nationals in the European Union, to whom we owe a duty. It is essential that we seek to negotiate a fair arrangement for them. I am afraid I do not want to give away the position on this issue today, when we have to protect that interest.

Q82 **Chair:** That is fine. That was helpful clarification. The second issue that is just worth picking up on for a moment is that you said that we would develop our own competition policy, which of course we will, because the competition policy of the EU is the one that applies now. Can you envisage that altering much from the legislation that we enacted on to our statute book in order to give effect to the EU legislation, which was itself legislation upon which the UK played a very considerable role in constructing? In other words, do we basically have the right competition policy on the domestic statute book now?

***Mr Hammond*:** We could have a long debate about this.

**Chair:** Do not let us do that.

***Mr Hammond*:** I personally regard some of the EU procurement processes as being burdensome and not conducive to the conduct of good and efficient public procurement, but I would certainly not agree with the direction in which Mr Mann appeared to want to travel. If I can extrapolate, it would have propped up uncompetitive and failing industries through public procurement, to the detriment of the taxpayer. We have been down that route before in this country. We know where it can go.

**John Mann:** It was not failing and uncompetitive, but successful and productive.

Q83 **Chair:** We are not going to go down there. I am asking a different question. It was very kind of you to bring us back to a rather different point that John Mann also made, but I would be grateful if I could have clarity in your answer to me on the point I did make, which is whether you are broadly happy with the legislation, with the exception of procurement.

***Mr Hammond*:** Beyond procurement, yes. We would want to introduce a regime tailored for our own requirements. In the absence of the external constraints that we currently have, for example on state aid, we would want to have a regime that allowed us to intervene appropriately, but restrained us from intervening inappropriately.

Q84 **George Kerevan:** Good afternoon, Mr Hammond. In February, your predecessor agreed a new fiscal framework between the Scottish Government and Her Majesty's Government, which basically said that there would be no detriment in the block grant adjustment. Can you guarantee to honour that agreement?

***Mr Hammond*:** The Government stand by that commitment, yes.

Q85 **George Kerevan:** Would you personally oppose, on principle, a separate trade relationship deal between Scotland and the EU?

***Mr Hammond*:** Yes. A part of a nation cannot have a separate trade deal. The United Kingdom will negotiate with the European Union as a united kingdom.

Q86 **George Kerevan:** We will broaden that. Can you see any situation in which the nations of the UK might have a different arrangement with the EU, in some sense?

***Mr Hammond*:** No.

Q87 **George Kerevan:** You said that Ireland would not have a hard border.

***Mr Hammond*:** No, I did not. What I said was that we have given a public commitment to the Irish that we will seek, in our negotiations with the European Union, to arrive at an outcome that does not require a hard border between the United Kingdom and the Republic of Ireland.

**George Kerevan:** You do not see that as a separate relationship for Northern Ireland from other parts of the UK.

***Mr Hammond*:** No, it is the United Kingdom's land border with the Republic of Ireland and the European Union that we are talking about here.

Q88 **George Kerevan:** Let me move on. What is the status of the Government's target to increase export sales of goods and service to £1 trillion by 2020?

***Mr Hammond*:** Stretching.

**George Kerevan:** Would you care to elaborate, to stretch your answer?

***Mr Hammond*:** It is a stretching target. It drives behaviour, but I would readily admit that we are a long way from delivering on that target, although of course one would hope that the recent decline in sterling, among other less beneficial effects, may have the effect of stimulating UK exports and UK exporters.

Q89 **George Kerevan:** To use your figure of speech, "stretching'", in fact for the last five years export sales have been broadly flat. Prior to that, though, there was a rise. That was boosted by the fall in sterling post the 2008 banking crisis. Even the rise of export sales then was nowhere near enough and it was broadly the same kind of fall in sterling that we have seen in the last few months. That generated nowhere near enough of an increase in export sales to reach your target, so I am just asking in what sense is a target to double export sales, four years from now, at all credible.

***Mr Hammond*:** It is stretching, as I said. We have considered this on a number of occasions and we have decided that maintaining the target, as a driver of Government behaviour and a driver of behaviour throughout the economy, is the right thing to do.

Q90 **George Kerevan:** Why in the last five years, given that export sales have broadly been flat, is the economy not responding? What is it that you are doing wrong?

***Mr Hammond*:** Do you mean why export sales have not increased?

**George Kerevan:** Why have export sales essentially been flat for five years?

***Mr Hammond*:** Sterling has been a strong currency over that period. World trade has slowed over that period. There have been some challenges around the areas where we have had the greatest comparative advantage.

**George Kerevan:** Basically the fault is external.

***Mr Hammond*:** I would not say the fault is external; it is structural.

Q91 **George Kerevan:** Okay, we will not quibble with that. If it is structural/external, what therefore is the validity of the target?

***Mr Hammond*:** The target is a driver. It is there as a driver of behaviour. We are seeking to engage more and more businesses in exporting. I am sure you know that one of our challenges is that we have a far smaller proportion of businesses, particularly SMEs, exporting than our comparator economies do. Encouraging small and medium-sized businesses to take advantage of the opportunities of exporting is one of the ways in which, over time, we will deliver high levels of exports.

Q92 **George Kerevan:** Can we expect that view to influence your Autumn Statement?

***Mr Hammond*:** I will reveal what is in the Autumn Statement on 23 November.

Q93 **George Kerevan:** I had to try. A final question in a broader sense about targets: the Government have failed in their major fiscal targets for budget surplus, debt-to-GDP ratio and the welfare cap in particular. You are also failing on house construction, which by the end of Parliament will be about a million behind your target. You are failing desperately on the net migration target, which is running at three times what your target was. You are failing on all these targets. Why bother with these targets if they are undermining your credibility so much?

***Mr Hammond*:** I do not accept that we are failing on all those targets.

Q94 **George Kerevan:** Which one are you succeeding in?

***Mr Hammond*:** The fiscal targets that you have quoted were clearly set in place around a certain number of assumptions. It was clearly understood, as with any set of fiscal rules or fiscal targets, that if the circumstances significantly change, the targets will have to change. That makes sense. Of course there is the option of squeezing a slowing economy to deliver a fiscal surplus target. I personally do not think that makes much sense. It is much more sensible to move the target.

We have been clear that we are not abandoning fiscal discipline. We have to live within our means. We have to get to budget balance but, given the uncertainty that the economy will now face over the next two and a half years, it would not be sensible to try to deliver that surplus in 2019-20, as my predecessor envisaged. You will be aware of the challenges that we face in doing that.

Q95 **George Kerevan:** My final question is: will you keep the same budget surplus target rolling forward? You do not need to say what it is, but can we expect a different fiscal rule come next month?

***Mr Hammond*:** You should not assume anything. There will be an announcement at the time of the Autumn Statement around our future fiscal plans.

Q96 **Chris Philp:** Let me start by returning to some of these European Union exit issues. You mention that the Government will not be providing a running commentary or revealing its hand, because it may damage our national interest, but would you accept that, equally, it could damage our national interest if we do not give businesses, and particularly financial businesses, enough clarity about our direction of travel? They may take decisions, in the next three or six months, about their own future arrangements. As Wes Streeting said, it might take a year and a half or two years for them to relocate staff. They cannot wait until the end of the process to know the position. They need to take decisions probably in the next six months. What can you say to those businesses that are considering their arrangements today to give them the confidence to stay in London, to stay in the UK and not to move operations elsewhere?

***Mr Hammond*:** You are right to identify a tension between the desire not to reveal a negotiating hand and the need to reassure businesses that are potentially affected by the outcome of these negotiations and, in some cases, have to make decisions before they will know the outcome of the negotiations. What we can do is engage closely with the businesses that are affected, not just financial services, but businesses across the economy that are affected by uncertainty. I have certainly engaged, as have my Ministers and officials, with the financial services sector.

Let me just make a couple of points. London is a global financial services centre. It is not just a UK and European Union financial services centre. Many US-based financial services businesses in London book all of their worldwide business outside the US through their London operations. London will continue to be a global financial services centre. Of that I have no doubt, and I do not think any of the players that I have discussed it with have any doubt. We are talking about a part of their business and how we are going to work with them to ensure that they are enabled to continue operating that part of their business from London.

Q97 **Chris Philp:** Yes, we are talking about a part. I recently met with the European chief executive of a US bank, which is in the top 10 globally, which now has 9,000 staff in the UK and 22,000 across Europe. His estimate was that, in the absence of passporting or an equivalent arrangement, about 10% of his staff would have to be relocated into continental Europe. I think that 10% is still a material proportion of London's business, which we should seek to protect.

You said a few moments ago, in response to John Mann, that you hoped and expected there would be reciprocal residence rights for migrations. Can you make the same statement in relation to financial services? Can you say, as you said to John Mann a moment ago, that you hope and expect that there will be a reciprocal arrangement allowing UK financial services businesses to do business in Europe and vice versa? You could say that to John Mann on migration; I hope you can say it to me on financial services.

***Mr Hammond*:** I certainly hope it and I do expect it, because I expect that, as we go into this discussion and as people look more deeply at these issues, some of the initial perceptions of national advantage that have driven some of the positions and attitudes that we have seen so far on this will melt away, partly for the reasons that have already been discussed in this Committee. If jobs were to go from London from the financial services centre, the likelihood that they would go to Europe is probably lower than the likelihood that they would either disappear altogether or go to the United States.

The damage that any erosion of the competitiveness of London's financial services market would inflict on the real economy in Europe, which of course is a big customer of real-economy-enabling services delivered through London, will also be a factor that comes into play. We are at an early stage of people across the European Union thinking through what the consequences here are. London is Europe's global financial services market. London provides a service to the manufacturing businesses, to the farmers and the commodity producers of the European Union. Anything that broke up this deep and broad pool of capital and expertise in London would be hugely detrimental to the real economy across the European Union, as well as to the UK.

Q98 **Chris Philp:** That is very helpful. Could I make two requests? Could I firstly request that the Government's rhetoric in this area emphasises the importance of maintaining these trade links, as much as it emphasises things like controlling immigration? Secondly, could the Government articulate that point—that it serves Europe's interests as much as ours to keep free trade going—partly to reassure firms here, but also to persuade politicians and the public in Europe that they should do a sensible deal, not a dogmatic deal to punish us? The more that those two messages could get heard, here and overseas, the better chance we have. I just feel that those messages are not being articulated or heard loudly enough, and I am just concerned about the implications of that.

***Mr Hammond*:** I hear your concern, and we will certainly seek to message in a way that reassures the industry. I do just need to be clear that the message we got from the British people on 23 June was that we are leaving the European Union and that we will control migration between the EU and the UK. Those are not things we can trade away. Those are defined parameters. Within those parameters, we will want to negotiate the very best possible deal we can for Britain's businesses and Britain's workers, including our vitally important financial services sector.

Q99 **Chris Philp:** I do not dispute the first two parts at all. I just think the third should be emphasised a bit more. Moving on to fiscal questions, in the past we have had quite a lot of ring-fencing of particular budgets, for example, effectively defence, overseas aid, the NHS, school spending and so on. Philosophically, what are your views on ring-fencing generally, particularly when you bear in mind that, in the last spending round, only 23% of Government spending fell outside the ring-fence, which gives the Chancellor rather little room for manoeuvre, particularly in uncertain times such as those in which we now live?

***Mr Hammond*:** It is true that we have a large amount of public spending ring-fenced. For good measure, I could add that we have a significant proportion of taxation locked, but these are commitments that have been made, either through manifesto commitments or through spending round decisions. I do not think they are up for reconsideration at this time.

Q100 **Chris Philp:** You have said already that the fiscal rule, which was the centrepiece of the previous Government's fiscal approach, has been removed in response to altered circumstances. Given that that, the centrepiece of the plan, can be removed in response to altered circumstances, should you not be similarly willing to at least consider altering some of these ring-fences also in response to precisely the same altered circumstances?

***Mr Hammond*:** I have no plans at the moment to reopen the spending review that was concluded and which essentially enshrines these ring-fences. I will say more about this at the Autumn Statement.

Q101 **Chris Philp:** I await it eagerly. I have noticed that 10-year gilt yields went down to 52 basis points in August, probably assisted by the Bank's quite generous monetary stimulus. Since then, they have more than doubled. Today, the 10-year gilt yield is 108 basis points. It has more than doubled in the space of two and a half months. Why do you suppose that is?

***Mr Hammond*:** It is not for me to second-guess the market but, if you read market commentary, part of it is a global phenomenon. Gilt yields have risen. Bunds and treasuries have risen at the same time, but UK gilts have risen differentially. That is certainly true. The conventional wisdom would be that that is a reflection of the falling value of sterling.

Q102 **Chris Philp:** Might it also be connected with the removal of the fiscal rule that we discussed a few moments ago, which may have partially undermined the market's confidence in our commitment to reaching a budget surplus in a reasonable timeframe?

***Mr Hammond*:** No, I do not think so, because the former Chancellor and the current Prime Minister both made clear at a very early stage that they did not believe that the fiscal surplus in 19-20 should now be pursued. There was no reaction to that in the markets. My own interaction with market players suggests that the markets are relaxed about that, so long as they are clear that our intention is to come back to a point of fiscal balance and that what we do in the meantime will be proportionate, measured and responsible. It is not some kind of splurge and I can promise you that it will not be some kind of splurge.

Q103 **Chris Philp:** I hope that is an important element of the coming statement because this year, as you know, we are going to issue £131.5 billion of new UK gilts. Should the yield on those go out by 100 basis points over five years, that will add about £6.5 billion per annum to our debt servicing. That is not a trivial sum. I think we should be mindful of the implication of our fiscal policy to debt servicing, because the market can be a pretty cruel mistress.

***Mr Hammond*:** Correct, it is not a trivial sum, but we should also bear in mind that, at every fiscal event for the last couple of years, we have seen lower-than-projected debt service costs, because of the falling yield on gilts.

Q104 **Mr Baker:** Chancellor, I would like to be helpful and I hope that will not provoke a heart attack. In contrast to some of my colleagues, I completely agree that it is right that you should keep information confidential. I remember back when I served in the Royal Air Force; if information was considered likely to be prejudicial to the interests of the country or possibly gravely prejudicial, it would be protectively marked "classified". Would you agree with me that some of the information, perhaps in relation to costs and benefits of particular options we might pursue, would be information that would be prejudicial to the interests of the country if it was released?

***Mr Hammond***: Some of the internal working documents would compromise the negotiating hand that the Prime Minister has in these forthcoming negotiations. I start from the rather old-fashioned view that Cabinet papers should remain private and Cabinet-level conversations should remain private.

Q105 **Mr Baker:** There has been some rather unfortunate briefing to and fro, which we picked up with Mr Scholar when he was before us and which you may be aware of. He was very insistent that if officials in any Department, I think it would be fair to say, were to brief against a member of the Government, it would warrant disciplinary procedures. Would you agree with that?

***Mr Hammond***: Absolutely, and I do not think anybody is suggesting that officials are responsible for briefing or leaking any of this material.

Q106 **Mr Baker:** It was reported in *The Telegraph* but perhaps we had better pass over that. I feel sure that you would share my dismay that any member of the Government or any official should brief against anyone else seeking to pursue the interests of the country.

***Mr Hammond***: Quite right.

Q107 **Mr Baker:** Turning to my favourite subject of QE, the MPC took a decision to increase the level of QE to purchase corporate bonds and to introduce the Term Funding Scheme. That meant that they needed to come to you for an indemnity. In deciding to grant that indemnity on this occasion, could you just tell us what factors you took into account?

***Mr Hammond***: I listened to the case that the Monetary Policy Committee had discussed. I looked at the expected challenges that the economy was facing already at that time. The uncertainty factor was already kicking in. I considered in the round the impact of the proposed monetary policy initiative, and sat that within when the broader range of options that might be available too. We have an independent monetary policy operating in this country. When the Monetary Policy Committee takes a clear view on something, it is reasonable to expect the Chancellor of the day to facilitate the implementation of that decision, unless there were any extraordinary, extenuating circumstances, which there were not in this case.

Q108 **Mr Baker:** Just to think about this potential for extraordinary extenuating circumstances, earlier on we discussed your appearance before the Lords Economic Affairs Committee, where you said, "The situation in the UK has been a toxic mix of increasing money supply and very constrained resource for building more houses, which is creating artificial asset price inflation." Can you foresee circumstances where you would take into account those circumstances when considering an indemnity for QE, in other words those broader extraordinary impacts on asset prices?

***Mr Hammond***: I was answering a specific question about the housing market there, lest the words appear out of context. What I have said already and will have to repeat here is that we respect the independence of the Monetary Policy Committee. We believe that the monetary policy arrangements in this country work; we have no plans to change them. What is clear is that we have other tools that can address the distributional consequences of monetary policy, whether that is distribution across the income curve, between generations or whatever.

One of the areas where a looser monetary policy has clearly had an impact is on the affordability of housing, but we have tools to address that. The Government's job is to use the tools that under our macroeconomic policy framework are allocated to Government to address any undesirable consequences of the monetary policy levers, which are allocated to the MPC.

Q109 **Mr Baker:** Clearly you made those remarks in relation to the housing market, but is this not, as we have just discussed, a material consideration when looking at the effects on the public of monetary policy? The Prime Minister has acknowledged it. You have acknowledged it, but you have asserted that this is really about other tools than monetary policy. Given that the Bank must come to you for that indemnity, are there any situations in which you can imagine turning down an indemnity because of the wider effects of QE?

***Mr Hammond*:** I am not going to get into a hypothetical exploration of how that process works. It is right that the Monetary Policy Committee reaches decisions on monetary policy independently. I would just like to say this: there has been a great deal of focus on the impact of monetary policy easing on asset values and the consequences for the distribution of wealth. That is all true, of course, and it is not incidental. That is the way the policy operates. An easier monetary policy in this country over the last six years has also delivered us 2.7 million jobs, and there will be a lot of people out there today who may not own assets, but will have a job that they would not otherwise have had. We have to look at the impact that an active monetary policy has delivered in the round and the benefit that is delivered to the economy in the round.

Q110 **Mr Baker:** I will refrain from getting into the arguments about the extent to which those jobs can last when they are based on credit expansion. In an interview, Andy Haldane said it was better to invest in property than a pension, for retirement planning. Would you agree with him?

***Mr Hammond*:** It is not for me to give investment or pensions planning advice, I am afraid.

Q111 **Mr Baker:** He did make that very point. House prices have risen 76% since the floor of the financial crisis, when annuities rates are down and returns on safe assets are down. Was Mr Haldane not just stating the obvious?

***Mr Hammond*:** One of the things that we have to just be a little bit careful about is talking about the housing market as if there is one housing market in the UK. Average house prices may have grown by a certain percentage, but there are still parts of this country—and Members around the table probably represent some of them—where house prices are now below their pre-financial crisis peak. It is not the case that there has been a uniform recovery across the country.

Q112 **Mr Baker:** Just thinking about that lack of uniformity, have you noticed a correlation between the distance of housing from London and the source of this new money through QE? There is a correlation between the rate of change in house prices and the distance from the City of London. In other words, if you live in London and the south-east, your house prices shoot away and, if you live farther away—if you are in the north-east, the north-west and Scotland—house prices tend to increase much more slowly. Have you considered why that might be?

***Mr Hammond*:** There might be many correlations with house prices that would fit better than that simple geographical one you have advanced, but I have not looked at it. If it would please the Committee, I would be very happy to go away and commission a piece of work on it and let you know what I find.

**Mr Baker:** I would be thrilled if you did, Chancellor.

**Chair:** Wes Streeting has one rejoinder. We are about to have a Division, so it might be interrupted and I think we will bring the session to an end with the vote.

Q113 **Wes Streeting:** Let us try to ensure it is not a case of saved by the bell. Following up on Steve Baker's question, and taking into account everything you have said this afternoon about not providing a running commentary and not undermining our negotiating strength and position, I can absolutely accept those arguments. Surely you must accept that, where we find ourselves now is Parliament, the public and obviously lots of business interests are effectively in the dark about the direction of travel. Would it not be reasonable at least to give Parliament some oversight and say in the opening position of the Government in its approach to the negotiations? That is not the same as red lines and everything else you have ruled out, but surely Parliament should have some say in what our opening position is.

***Mr Hammond*:** The public, parliamentarians, business and everybody else have a very clear idea from what the Prime Minister has said. We are leaving the European Union. We will be introducing controls on migration between the EU and the UK. We will seek the very greatest degree of access to the European marketplace for Britain's providers of goods and services. That will be our objective in this negotiation.

Now, of course it is not just about us sitting here in a locked room and unilaterally deciding what we want the outcome of this discussion to be, because it is a negotiation and it will involve give and take along the way. I am very clear that we have set out our objective for the negotiation to deliver the greatest degree of access that we can achieve for Britain's providers of goods and services. I do not want, because I do not think it will be helpful to us, to constrain the Prime Minister any more than is absolutely necessary in her negotiating a position. I want her to have all the tools available to her. I want her to have all the options open, so that she can engage with her interlocutors, hear what their position is, explore where there are options to find mutually acceptable solutions and try to take this forward in a constructive way.

There has been quite a lot of position-taking, as one would expect at this stage in the negotiation, but I remain optimistic that there are, at very senior level across the European Union, some deeply pragmatic people who have shown by their actions, time and again, that they can find solutions when challenged with problems. If we look at the history of the European Union, how many times have people said, "There is no way through this problem or that problem," and yet the European Union has been able to find a way through it? I hope that pragmatism and engagement will deliver us a mutually beneficial solution, because I think it will clearly be in the interests of the people of all of Europe, including the UK, if we continue to trade closely together and work closely together, after we have left the European Union.

Q114 **Chair:** That is a very interesting reply, which I am sure we will take a close look at. In the time remaining, which is very brief, I just want to ask you to look at one issue that has caused the Committee a good deal of concern in the past year and caused the Committee a great deal of happiness in the preceding five years. In 2010, we asked George Osborne, as the new Chancellor, to publish a distributional analysis of each of his major fiscal events. He thought about it carefully, came back and did so, and he explained the need to put this on a consistent basis, so that we could have a running view, as no distributional analysis is perfect, but it is of great value if it is done on the same basis year on year.

In 2015, immediately after the general election, he changed that basis and refused to publish it. This question is being extended in order to give you a moment to read the briefing note being passed to you. Rather than take a decision now, would you be prepared to take away this issue and think carefully about it? It got your predecessor's relations with this Committee off on a very good note in 2010 that he did this, and it might just do the same for you, if you feel able to resume publication of that series.

***Mr Hammond*:** Obviously I would seek to have an excellent relationship with the Committee.

**Chair:** We are very glad to hear that.

***Mr Hammond*:** I am aware of the issue. As you have said in your remarks, Chair, no distributional analysis is perfect. There are all sorts of challenges around distributional analysis and you are very well aware of the weaknesses that my predecessor identified in the previous way the data was presented. What I can say to you is this: I will publish a distributional analysis and I will look carefully at the best format for doing so, including the issues you have raised around the baseline.

**Chair:** And the value in the continuity of the series.

***Mr Hammond*:** I will consider all of these issues that you have raised.

**Chair:** Thank you very much, Chancellor, for coming before us. It has been extremely interesting and we look forward to seeing you very shortly, after the Autumn Statement.