HOUSE OF LORDS

Select Committee on Economic Affairs

Corrected oral evidence: The Economics of Higher, Further and Technical Education

Tuesday 10 October 2017

3.35 pm

Watch the meeting

Members present: Lord Forsyth of Drumlean (The Chairman); Baroness Bowles of Berkhamsted; Lord Burns; Baroness Harding of Winscombe; Lord Kerr of Kinlochard; Baroness Kingsmill; Lord Lamont of Lerwick; Lord Layard; Lord Sharkey; Lord Tugendhat; Lord Turnbull.

Evidence Session No. 1 Heard in Public Questions 1 - 13

Witnesses

I: Rt Hon the Lord Willetts; Paul Johnson, Director, Institute for Fiscal Studies; Rt Hon the Lord Adonis.

Examination of witnesses

Lord Willetts, Paul Johnson and Lord Adonis.

Q1 **The Chairman:** Lord Willetts, Paul Johnson and Lord Adonis, I think you know everyone here. Welcome to the Economic Affairs Committee. As you know, we have sought to have a broadly-based inquiry looking at the issues of value for money for the taxpayer, value added to the economy and the benefits to students across the board. We will try to leave the more tabloid issues, such as vice-chancellors' pay, to those down the corridor. Over the next six months, we hope to produce a pretty comprehensive report.

Today, we are going to look at the overview of student finance. There is certainly a broad range of views among the three of you, and I hope you will feel able to share those with us in detail. First, is it a concern that it is estimated that about one third of graduates are in jobs that do not require university degrees?

Lord Willetts: I would obviously prefer it if that were a lower figure. However, a lot of graduates are on a trajectory through the labour market where, even if for a time, especially when they are younger, they are not in a "graduate job", they have a very high chance of securing one eventually. Those statistics are quite hard to measure accurately, because one of the things going on is that jobs that remain unchanged in the official standard occupational classifications are becoming more demanding; their characteristics are changing. One estimate is that about 40% of graduate moves into graduate jobs are as a result of the job itself changing. A lot of work is becoming more complicated. There are more complicated regulations to comply with and more complicated technologies to use, and graduates seem to change the nature of some of the work they do just by virtue of their extra skills.

Paul Johnson: I broadly agree. In that number of a third or so, it is very difficult to understand exactly what is and is not a graduate job.

The Chairman: It is the anecdotal point about people with degrees ending working up at McDonald's.

Paul Johnson: Exactly. There are different sorts of those things. Clearly, ending up in McDonald's is a very different thing from ending up in a job that gives you a real chance of moving up within an organisation. We know that there are some externalities associated with being a graduate for both the employer and the employee. As David said, these jobs are changing over time.

All that said—this relates to questions you might ask later—there are some clear mismatches between the kinds of skills coming out of universities and some of the demands in the labour market. Clearly, there are people who have spent time in universities who are doing jobs that do not require the particular set of skills they may have learned, or the particular degree. One should probably think of it in a broader sense. What is the higher education system trying to achieve? How does it match labour market outcomes, and how does it relate to the other routes that people could take? If the question is whether feasibly there was a better set of skills that some of those people could have got that would better match the labour market, the answer is almost certainly yes. How you get there is a rather more difficult question.

Lord Adonis: The understanding of graduate careers changes over time, and it is not all one way. I am very struck by the fact that, under the impact of the very high fee levels at the moment, quite a number of careers that over the last generation have become graduate careers are now starting to move the other way. Many of the big accountancy firms are now recruiting as many high-level apprentices as graduates. Indeed, the Civil Service itself has now started recruiting, essentially, fast-stream apprentices who are doing jobs that fast-stream graduates have done hitherto. I met a group of them a few weeks ago. It is quite striking that 18 or 19 year-olds who even a few years ago would definitely have thought of going to university are now seizing prestigious high-level apprenticeship opportunities as a way of going straight into careers without having to take degrees and take on debt. I see no reason in principle why that could not go a lot further.

I see no reason in principle why the Civil Service could not recruit as many high-level apprentices as it does graduates. I see no reason in principle why accountancy, and even the law, which, if you go back two generations, were not graduate careers for many of those participating in them, could not once again become much more vocational careers, where people can train on the job, get qualifications that are recognised in their profession and not have to take on high levels of debt. That is much more the case in German-style economies where the number of graduates is much lower to start with.

Lord Lamont of Lerwick: On Lord Willetts's phrase about lots of graduates being on a trajectory to a better job and 40% of graduates moving, might not the same happen if they did not have a degree?

Lord Willetts: That goes to the fundamental question of whether we think that going to university changes people. My view is that the evidence shows that it does. I am rather struck by the way in which advocates of the early years have been so persuasive about the first three years mattering for people's development. I think the three years at university also change people, and I suspect—more than suspect—that going to university gives you training in critical thinking that enables you to move between jobs with different characteristics. Although there are some sceptics, such as a Member of this House, Baroness Wolf, who says it is all just signalling, the overwhelming evidence is that going to university is more than that; it is like three years of school education. You learn stuff and develop new skills.

To take the Civil Service as an example, when I arrived in the Treasury there was a deputy secretary who had started as a clerk. That was the fantastic route he had taken. Nowadays, it is more and more difficult to see people emerging at the top of an accountancy firm or the Civil

Service with the kind of skills needed unless they have had either a period at university aged 18 or, during their career, have been sent and funded to do higher education in some other way. I do not think that stopping our education at 18 is the basis for doing a lot of the significant jobs in Britain today.

The Chairman: Baroness Wolf's point is that, if you increase the number of people with degrees, it risks raising the qualification barrier to jobs that could be done otherwise without a degree.

Lord Willetts: That is what she says. The evidence cuts both ways, but intuitively I think it is unlikely that three years at university, any more than three years in prison, or three years in the Armed Forces doing national service, does not change you. The idea that we can educate people up to the age of 18 but when they go to university it is all just a matter of signalling stuff is implausible. During three years at university you learn new concepts, you broaden your horizons and you develop critical skills. Most countries in the advanced West have seen a growth in higher education, and it seems to be associated with improvements in productivity in a modern economy. There are different estimates, and learned economists make those estimates. It seems to be a driver of productivity. At each stage of the growth of higher education participation, from 5% to 50%, we have always said that it cannot possibly go any further and surely it has gone too far; but at each stage it has kept going and, by and large, it has transformed the British economy for the better.

Q2 **Baroness Kingsmill:** My question was covered very much by what Lord Adonis said. I am curious to know whether you felt that the amount of debt meant that people were discouraged from undertaking university education and whether our economy suffered as a result.

Lord Adonis: If you talk to sixth formers and those making decisions at 18 or 19, it is undoubtedly true that they are looking at alternatives to university in a way they were not a few years ago. As the number of high-level apprenticeships increases—I think the number will increase dramatically with the apprenticeship levy, which is providing significant funding for companies to offer them—they will become increasingly attractive. People not only save £60,000 worth of debt and, given 6.1% interest, up to £100,000 that they might have to pay back, but they are earning at the same time and they have a secure job. I suspect that we will see trends in both directions over the next few years. It will not by any means be just a trend towards more graduates.

Baroness Kingsmill: Do you think there is any argument for doing as they do in the United States? Where there is a shortage in the public sector of, say, teachers, doctors or even nurses, and given that such a high proportion of students will not repay their student debts, is there an argument for saying that if graduates agree to work in those areas they could be forgiven the debt entirely?

Lord Adonis: When I was schools Minister, I tried hard to persuade the Treasury of the virtues of that argument. I did not get very far because it was convinced that, as soon as it conceded it for teachers, nurses would be the next in the queue, local government officials would not be far behind, and it would be left with almost no debt to collect.

Baroness Kingsmill: Is it not right that approximately 85% of it will not be collected?

Lord Adonis: The Treasury is not keen. There would be great difficulty in trying to work out what the rules are going to be. How many years do you have to teach to get your debt written off? How much do you get written off?

Baroness Kingsmill: In the States, they manage to do that. There is a percentage. For five years, you are forgiven half; for 10 years, you are forgiven the whole lot.

Lord Adonis: In education, we have shortages in some areas, in particular in STEM secondary teaching subjects. We do not have a shortage of primary school teachers, so where you draw the line would be very controversial. These issues are not easy to wrestle with.

Paul Johnson: To respond to your first question, there is no evidence in the data that the fee system has had much effect on the numbers of people going into higher education. It is important to understand that. There may be an effect later on, and a group of young people may be making different choices, but overall, as far as we can tell, the numbers have not been affected. Even more importantly, as far as we can tell, there has been no reduction in the numbers from lower socioeconomic backgrounds going to university.

Related to that, if we are talking about the breadth or scale of higher education, one of the dangerous arguments for having fewer people going into higher education is that, if you reduce the numbers, almost certainly it will be those from lower socioeconomic backgrounds who get cut out. That will be the effect, and we have to be very clear that there is an adequate route for them.

On the question about whether you forgive the debt for certain public sector workers, there are two things. First, it is almost certainly more effective just to pay them more. I do not know why you would do it in a roundabout way by forgiving debt. Let us not kid ourselves that public sector workers are the lowest-paid graduates, because they are not.

Baroness Harding of Winscombe: Lord Willetts, it is obviously true that three years changes you whatever you do. Is not the debate about whether, for at least a proportion of young people going to university today, their three years at university is the most effective way of preparing them for a successful and fulfilling life, rather than some form of vocational or further education route that is probably not three years in one stretch but builds a different set of skills? I was very struck by your statement that flexible labour markets are driving a very weak vocational FE sector in the UK. That really did not ring true to me in the modern world. I do not think people are taking coding courses and becoming coders as protection because it is a restricted market. How should we be thinking about the tipping point—the balance between HE and FE?

Lord Willetts: Ultimately, that is a matter for personal decision. I do not believe in government setting targets for the number of people who go to university. I believe young people should have the information and evidence to make a choice for themselves. I am not surprised that a lot of them voluntarily choose to go. I very much agree with Paul Johnson's point. I used to have this argument with Vince Cable when we were talking about number controls. In my former constituency, 23% of young people went to university; in his affluent Twickenham constituency, the figure was 63%. If the only way we can get more people from Havant going to university is to have fewer people going from Twickenham, we will have a very long wait. That is one of the other arguments for expansion.

The structure of the economy is also a fundamental issue. We have already heard from Lord Adonis a reference to the German model. The German educational and industrial models are closely linked. In a highly regulated labour market, with a large amount of licence to practise that you need to secure to do a whole range of jobs, and apprenticeship routes into those jobs, and provincial banks funding the companies that protect those jobs—in other words, a much more corporatist model—you can also have a whole series of regulated training routes into specific types of vocational employment. Sometimes the higher education debate is just the lightning rod for a debate about what kind of structure we think the British economy should have. The US and the UK are countries with highly flexible labour markets, relatively low levels of apprenticeships and relatively high levels of university participation, where there are many fewer guaranteed routes into secure regulated activities, and where people need generic skills and are expected to move around during their career. It is no accident that liberal labour market economies of the sorts I believe in also tend to have high levels of university participation and low levels of apprenticeship.

Lord Lamont of Lerwick: I am instinctively on the side that Lord Willetts is advocating, but I want to be more convinced. As Baroness Harding said, obviously all three-year periods change people, but, to be brutal about it, if somebody studies medieval art, which I am all in favour of them studying, why is that going to equip them better in the immediate post-university period than doing a management trainee course in a firm, being in the Army or something like that?

Lord Adonis: That is an extremely good question.

Lord Willetts: We could have a system in which we specified how many places there were at university for different courses. I would have two objections. First, I believe in the autonomy of universities; I do not believe in government manpower planning deciding how many medieval art historians we need as against management trainees. Secondly, the evidence is that the training you get is of some value. I believe that the most widely studied course among chief executives of FTSE 100 companies is history. You may say that reflects badly on the performance of British industry, but my view is, fair enough. If that course has ended up producing people with the necessary skills, or they learn other things later on, fine.

That is where Robbins, another free market economist, was right. If I cannot persuade Lord Lamont, let me try to do it via Robbins, who was a distinguished neo-classical economist. He asked how we should plan universities. How should we think of universities? Should we try to predict the jobs that people are going to do in 20 or 30 years' time and allocate places at university in accordance with our predictions? He said, "No, we cannot know". Instead, he wanted an open, flexible system, heavily influenced by the number of people with the capacity to benefit from higher education.

Lord Adonis: I confess that I am a historian. When Robbins was producing his report, 5% went on to university. We are now in a very different world where, by the age of 30, approaching half have gone to university. This is a completely different world. The issue is not whether three years studying the history of art might or might not be advantageous. The question is precisely Lord Lamont's question, which is whether, if you are pretty clear what you want to do and which direction you want to go in and it is a commercial occupation, it is better to learn on the job and not accumulate between £60,000 and £100,000 of debt and be less work-ready at the age of 21 than you would be if you started at 18.

Although it is absolutely correct, as Mr Johnson said, that we have not yet seen numbers turning down, it is by no means clear that the increase in the number going to university is relentless. Young people are very able to do the calculations. When they are making calculations about having debts approaching £100,000 and having a job that could pay them between £20,000 and £25,000 a year, I think they will start wising up quite fast.

Lord Turnbull: I accept the point about choice and people having information, but is there not a huge information disjunction? The university offer is very well known. People know it and can see it. What is more, you just go round the corner and you get the money immediately. The offer down the other channel is deeply confused and very fragmented. My proposition is that the universities have exploited that. They put forward a very recognisable product and people are tempted to go down the university channel when possibly their best interest is to go down the other channel. Universities and schools are not applying the principle, which is now required of financial institutions, of knowing your customer. They are not advising people the best channel to go through. Are you aware of any study that takes two groups of people at 18, one of which goes through the non-university channel, working and getting some apprenticeship assistance and the other goes through the university channel? Where do those groups end up when they both get to 30? I suspect that a lot of people who now go through the university channel would be better off going through the other channel.

Lord Willetts: The evidence so far—the world could change—is that for people of comparable academic achievements at the age of 18, comparing the ones who then go to university and the ones who do not, the ones who go to university subsequently earn more and have in many other ways better lives, with improved life expectancy. That evidence comes from work done by Professor Walker, published by BEIS in my time as a Minister. It also goes back to twin studies and all the classics of social science; it goes back to US studies of marginal students getting into university and people who did not; it goes back to US studies of the Vietnam war when some people were selected for the draft and some people avoided it by going to university. A whole host of studies shows that there is a gain.

I agree with your point that other routes need to be clearly signalled, but I expect that in a modern western economy the managed transition to adulthood via three years of higher education is the mainstream route people will take. The danger of some people going down the alternative route is that I know who they will be. Eton will not be sending 25% of its kids on apprenticeships. You will reopen the social divide in participation by advantaged and disadvantaged groups. We can already see it. If there is a social problem of too many people going to university, it is not a problem in Hull, Blackpool or Bolton where they have 20% participation; it is in Hampshire and Surrey, where they have 60% participation. If we are to send out a message about doing something different, we should be sending it to the boarding schools and the elite academic schools of the prosperous Home Counties. That is where the social problem is most acute.

The Chairman: Paul Johnson, the IFS is looking at the LEO initiative.

Paul Johnson: The Department for Education data arrived at the IFS last week, so we have not yet analysed it. David's take on the literature thus far is essentially correct. Of course, that is for previous generations and things may have changed, as he said. It is clear that there are some universities and courses where the pay for those coming out of them is pretty low. I suspect there is more work to be done to look into that and understand it. One almost squares the circle. I am with the idea of having a free choice and a free market, as David puts it, but Lord Turnbull is also right in saying that there is not a level playing field. It is incredibly difficult to navigate the non-university route and incredibly easy to navigate the university route. That is not a problem of the universities; it is a problem of the rest of the system, which just does not work. I see that as a parent as well as an analyst of this stuff. It is the other side of it that needs to work.

Lord Sharkey: I declare that I am a council member of UCL.

There has been a change in participation rates that has not been mentioned so far, which is in part-time and mature students. Since 2010, HEFCE shows there has been a 61% decline in the number of part-time students. It also shows that that is probably an effect of tuition fees. Is this something we should be concerned about, and, if it is, what is the remedy?

Lord Willetts: Yes, and I have to accept that it is one of my biggest regrets about my time as Minister. Contrary to Baroness Kingsmill's fears, thank heavens when it came to 18 year-olds going from school and college or university, they understood it was a repayment system through PAYE and they were not put off, but part-time students were. What has happened is very regrettable. The lesson I learn from it is that, rather than the seductive idea that you can have a single pot per person to pay for their education, you need different models for different groups. We extended loans to part-time students thinking it would have the same beneficial effect on them as the loans for full-time students, and all would be fine. The evidence is that the loans for part-time students have not worked. There has been low take-up and people have been put off. We need new mechanisms for helping adults to study part-time, and I accept that the loan model has not delivered for them.

Lord Sharkey: Are there any remedies?

Lord Willetts: If—I underline that—at any point we were looking at how to spend limited public money and what public spending would do, rather than spending it on compensating universities for a general reduction in fees, I have a list of things where I think there is a need. Certainly, a public spending package for adult learners, including helping mature students with the cost of tertiary education, be it university or not, would be a high priority.

Lord Kerr of Kinlochard: I have three questions, the first to Mr Johnson. You said the numbers showed that the disadvantaged in society—those coming from poorer backgrounds—were not being deterred by the loan system. In your view, will they be deterred—it is too soon to say—by the abolition of maintenance grants? Is it not likely that, with means-tested loans replacing grants, the prospect is that those coming from disadvantaged backgrounds will face a higher load of debt than those from wealthier backgrounds?

My second question is to Lord Adonis. I think the IFS is saying that the costs to the taxpayer of higher education are now greater than they were before Lord Willetts's 2012 reforms, so we need to look for some other justification for these reforms. Is it a market that works reasonably well?

Finally, my question to Lord Willetts is about his written evidence, for which I was very grateful. It was not the labour market bit of it that puzzled me, but the productivity argument. Lord Willetts tells us, "A 1 per cent increase in the share of the workforce with a degree increases long-term productivity by between 0.2 per cent and 0.5 per cent, so a third of labour market productivity growth from 1994 to 2005 can be attributed to rising numbers of graduates in the workforce". I wonder. I am with Lord Lamont on this. If that is right, why do we have such a big productivity problem? Lord Willetts spoke about the German economy and how it works on a very different model. It appears to have, from a much lower proportion of graduates, a much higher productivity rate.

I believe that university changes people. I am with Lord Willetts to that extent, but my idea of university is like Newman's whom I saw Lord Willetts quoting the other day: the idea of university is to teach students to think, read, compare, discriminate and analyse. Stop. I look at your productivity argument and I think you are clutching at straws if you are trying to defend higher education on the basis of British productivity records.

Paul Johnson: I will answer the question about maintenance loans and grants. We do not have clear evidence yet about the move from grants to loans, but we know that the up-front availability of maintenance money is a really important part of what determines whether poorer students in particular go on to higher education. To the extent that we know anything, it suggests that loans, in the way they currently exist, and grants are pretty good substitutes for each other, in part because of the form of the debt. Although in principle they have a higher level of debt, in practice it will not make any difference to the amount they pay back. The crucial variable is not whether it is a loan or grant, but the level at which it is payable.

Lord Adonis: On the issue of markets, of course there is no market. There is what I term a cartel. All universities charge £9,250 for virtually all courses. We see how the cartel works, because, when the maximum fee level was increased this year from £9,000 to £9,250, almost overnight all universities went directly up to £9,250. All the evidence is that, if the figure had gone up further, they would have gone up higher still.

This has led to—how can I put it?—a vigorous debate between David and me. When he was the Minister responsible, he gave an assurance to the House of Commons that it would be highly exceptional for universities to charge more than £6,000, and he said that the Government would intervene if what he termed lower-ranking universities charged more than £6,000. They all went up to £9,000 and he did not intervene. What he now says is that it was foolish of him to think they might not have charged £9,000, because this is a positional good and by charging less universities would simply be signalling that their degrees were less valuable. He has now extended the argument further, in a way that I find, frankly, astonishing, which is that it would be a betrayal of social mobility and social justice if London South Bank University and London Metropolitan University charged less than £9,250 because that would signal that their degrees were less worth while and they were investing less in students from lower-income families than higher-income families.

I take almost a Tory view of these things. People should get what they pay for. If you are not getting remotely close to £9,250 of value from your degree, which I venture to say you are not from London South Bank University reading sociology, you should not be required by the cartel that operates between universities at the moment to pay that. I very much hope that the Committee will take up that issue. My view is that a lot of graduates are being saddled with high levels of debt in a cartel where they have no option, if they go to university, but to pay very high levels of fees that are not even justified by the cost of their courses, let alone by the return they will make as graduates from those degrees.

The Chairman: Why do you use the word "cartel"? That word implies a particular pattern of behaviour. Surely, if 83% of students will not have to pay back the money in full, and you are producing a course that is not going to provide perhaps the highest incomes and, therefore, students may not pay anything back at all, it is entirely logical that the universities would exploit the fact that this money was available for free and to no disadvantage to many of the students. Why is it a cartel?

Lord Adonis: The truth is that we do not know, because no universities have charged lower fees. It is received wisdom—

The Chairman: I am just making the point that they are behaving entirely rationally.

Lord Adonis: I am not sure that they are. That attributes a very high level of stupidity to graduates who think that the fact they will have to pay back those very large sums is not something they should worry about because it is all in the future. In my experience, students are no different from others. You do not take out a mortgage on a £1.5 million house rather than a £500,000 house on the grounds that all the payments will be made 20 or 25 years hence; you have some regard to price and value.

The Chairman: Paul Johnson, you were shaking your head vigorously.

Paul Johnson: It is simply wrong to refer to it as a cartel for exactly the reasons you describe. The universities are rationally responding to the structure set up. Perhaps not ex ante but certainly ex post, it was obvious they would respond to it by charging the maximum. Why would they not? A low-income graduate simply does not pay it back. If you were to reduce the fee from £9,000 to £6,000, it would be of no benefit to most graduates. That means there is not a market. Almost by design there is not a market, at least in terms of price. Clearly, there is some kind of market in the sense of people making choices about where they go.

It is also worth thinking about what the reverse situation might be. Suppose we were in a world where there was a market in which Andrew's least favourite university, by the sound of it South Bank University—

Lord Adonis: I like it a great deal. It just should not be charging £9,250.

Paul Johnson: If it was charging £6,000 and somewhere else was charging £9,000, and as a result a whole group of low-income students were going to South Bank and not a university Andrew does like, that would be a situation in which social mobility was compromised. What we do not have is a market that is working on the basis of price, but we also do not have a cartel. We have something that allows social mobility to occur, and if we had a proper market it would not.

Lord Willetts: I think the clerks were right to sit Paul Johnson between Lord Adonis and me. As some views have been attributed to me, I would like to comment on them before answering Lord Kerr's questions.

Once you have a graduate repayment scheme of the sort we have, you do not have price competition, but one of the other things we were able to do was to remove number controls. In the days when this was public spending, the Treasury controlled public spending on higher education by allocating a fixed number of places to each university down to the last digit. To stick with Lord Adonis's example, South Bank would be given a number. Now that it is not public spending, the Treasury is no longer controlling numbers, which means that universities students want to go to are growing and universities that students do not want to go to are shrinking, and more students are getting their first choice of university. We have a highly competitive situation, but it is indeed not competition on price.

On the argument about London South Bank, as we went through that debate, I commissioned economists at last to access the full data from HMRC on graduate earnings. Anna Vignoles, Neil Shephard, the IFS and others published that report. The question was: do we have evidence of a high-performing university? Are people earning more because of higher value added at their university? I stand to be corrected by Paul Johnson if this is an inaccurate summary, but they found that once you allowed for the prior attainment of the students when they arrived, and their social background, there was no further institutional effect of any significance.

I suspect that most people in this room have an implicit judgment that Oxford is better than South Bank. That is above all because of its global research excellence, and is based on the performance and prior attainments of the people it recruits. If that research had shown something different—that there was a very clear measure of value added not explained by prior attainment and social background—I think I would have drawn different policy results.

Finally, think of this as a secondary school. There is a secondary school in Oxford that takes predominantly white middle-class kids, many of them privately educated, and there is a secondary school in south London taking much more ethnically diverse students with lower levels of attainment and much tougher social backgrounds. In the school debate, we proudly talk of the pupil premium we send to the secondary school in south London to compensate for the fact that it is taking on a tougher educational challenge. It would be odd to do a kind of reverse pupil premium in higher education.

Lord Adonis: That is an entirely false analogy, because it is the state that pays the pupil premium for the school in south London, whereas David is expecting the student to pay for the student premium in the case of South Bank University. If you gave students the option of being able to go to South Bank University and pay half the fee rather than paying more of the fee so that they can claim their university is costing as much to offer its degrees as the University of Oxford, I know pretty well which course the student would take. I am sorry to sound like a Tory in this argument.

Lord Willetts: That is why it is right to have a graduate repayment scheme. If people emerge from university and are not earning much, they pay back less; if they are earning more, they pay back more. The best way to make this progressive is to know what they are earning.

I owe Lord Kerr an answer. One answer looking around this group is that these are Treasury figures, and what could we treat with more reverence than that? Maybe that is not a totally convincing argument, but when the Treasury tried to estimate productivity performance in the UK in the period when we had a fantastic run, it attributed it to an increase in the number of graduates in the labour market. Indeed, when the OECD is looking at the long-term growth prospects for economies, one of the factors it uses is the proportion of graduates in the labour market.

At the moment, since the crash, all the figures for every stage are worse. The relativities have barely changed; in other words, there are still advantages in being a graduate as against being a non-graduate, but it is absolutely the case that everything is worse since 2008, including probably the absolute but not the relative graduate premium.

Although I talk about the economic benefits of university, I quite agree that there are non-economic benefits as well. The quadrant axis is a very good way of thinking about it. There are economic and non-economic benefits, there are individual benefits, and there are social benefits. That gives four types of gain. There is empirical evidence for each, and the relative weight we attach to them can be a matter of personal value judgment.

Lord Kerr of Kinlochard: You are not meeting Lord Lamont’s point. They might just be brighter people. It might not be the fact that they have a degree. Nor are you meeting my point. If they are Treasury numbers, of course they take no account of comparisons abroad. The Treasury never looks across the channel, but why are the Germans and French getting much higher productivity numbers than we are? Why are you taking credit for additional graduates and saying that equals more productivity, when they have fewer graduates?

Lord Willetts: On Lord Lamont’s point, the economic evidence I am citing varies, but most of it tries to do a proper comparison with a relevant counterfactual. When the figures for the graduate premium are cited in government reports, including research I commissioned, that is not graduates versus everyone else; it is graduates compared with as tightly defined a group as modern economics can come up with; they would be similar in all other respects but they did not go to university. We are not talking about just a selection effect; we are trying to capture effects as a result of going to university. Not every report does that, but the serious ones do.

Paul Johnson: On productivity, there are two really important points. One is that, looking historically at the period through the 1990s and early 2000s, there is pretty solid evidence that the increase in education through universities played a significant role in UK productivity performance, but the most recent work we have done, and some work in the US, suggests we may be at the turning point where that increase is no longer there. It may be that we have got to the point where the proportion of graduates in the labour market rising will no longer have that effect. There is some work we published earlier this year to that effect, which corroborates the idea that it was positive until mid-2000 but may no longer be so.

Lord Lamont of Lerwick: I want to ask Lord Adonis about the lack of price sensitivity and whether there is a market. Does he think that the reforms, by which I mean the increase in fees, plus the removal of the cap in numbers, not only give an incentive to charge the maximum, whatever the course is, but provide an incentive to recruit overseas students? It is a great benefit to us to have a link with people overseas, but those students are charged very large amounts of money for courses that perhaps are not always value for money.

Lord Adonis: The overseas student fee is not regulated in the same way and is not subject to the cap. Universities have a strong incentive to recruit overseas students from outside the EU.

Lord Lamont of Lerwick: That is my point.

Lord Adonis: But they would have just as strong an incentive if there was a market within UK students. Indeed, they would probably have a stronger incentive because, if there was a market, there would be more universities charging less than £9,250, so the margin they would make on overseas students would be higher still. While we have the current cap level, the incentive to recruit overseas students is strong and growing. My own view is that that is probably a good thing, because there clearly is an international market for students.

Lord Lamont of Lerwick: But are they getting value for money?

Lord Adonis: They have a choice, do they not? They do not have to come here. There are other very strong international providers of university education in the States, Australia and continental Europe, including others in Europe teaching in the English language—for example, the Netherlands. I am much less concerned about that, because if we were overcharging international students they would quite rapidly start to go elsewhere. We seem to be pretty price competitive with other major international education providers, and less expensive than many of the providers in the United States.

On the issue of the cap and the cartel, when I was engaging in a debate with the Competition and Markets Authority on this and trying to persuade the CMA to take it up, I was trying to develop the concept of a tacit cartel. I cannot produce for the Committee emails between the University of South Bank and the University of Oxford agreeing that they would both charge £9,250. However, having been an education Minister and an education journalist, I know that these people meet the whole time. Universities UK is a social club as well as a business club, and the idea that they do not discuss what they are going to do in respect of fees, and have not done so since the advent of fees in 2004, is farcical. It is very clear to me that there is a tacit cartel operating that is profoundly against the public interest, and it should have been stopped in the way David said he would stop it, if it had developed after 2010.

The Chairman: I think we have covered that. In fairness to London South Bank, I should point out that it was the *Sunday Times* and *Times* university of the year for graduate employment.

Q3 **Lord Tugendhat:** As I understand it, the primary goal of the 2012 reforms was to improve the quality of students' academic experience and increase their educational gain. How does one measure that? Is it being achieved? If you feel that it is being achieved, by what measure is it achieved?

Lord Willetts: It is hard to measure, and that is why this debate is so frustrating. Although we can measure research excellence and the prior attainment of students, the teaching experience during their time at university is very hard to measure; it is one of the reasons why the Government are now bringing in the TEF. We can look at the national student survey and surveys of student engagement. During the time we brought in those changes, student satisfaction went up. Although it is an imperfect measure, we can look at teaching staff-student ratios—not at all staff. I am afraid that the story that tells is a rebuke to all of us. It tells us that for 20 or 30 years, even as staff-student ratios in schools were improving, in universities they were deteriorating, because, when faced with devoting public funding to universities, successive Governments gave it a low priority. Since the changes came in, the staff-student ratio in universities has improved. We can find some indicators, but I am absolutely with the people who are keen to have more indicators.

As to why we did it, this is, essentially, a repayable education voucher for higher education. It is a system where a student takes their voucher to the university of their choice and then repays it if they can afford to. I believe that as a point of principle and theory that is a better way of doing it than the Government's allocating public expenditure university by university, but, let's face it, there were also public expenditure demands. We had to reduce public spending, and this compensated, and slightly more than compensated, universities for the loss of public spending in grants. The reason it was slightly more than compensation was that for 20 or 30 years they had had declining real resource per student, so it corrected a bit of the historical decline over the past 30 or 40 years in public resource per student in higher education.

Lord Adonis: The national student survey shows high levels of students and young graduates who do not believe they get value for money for their courses. It is now up to about a third, and it has increased in each of the past five years. Although it is true that there are high levels of overall satisfaction, it is not the case that there are high levels of student confidence in the value for money of their course. My view is that that is a perfectly sensible judgment, because I have seen no evidence from universities that a high proportion of the courses they offer cost anything like £9,250. I would be interested to see the evidence that the Committee takes from the universities. They will not publish accounts showing, course by course, how much each costs and what proportion of the courses they offer costs the same as or more than the actual fee level. To my mind, that is a matter of great concern, because I see no reason whatever why students should have to pay more than the actual cost of their course for their degree and be saddled with very high levels of debt. That is giving rise to the growing level of concern among students and young graduates that they are not getting value for money.

Lord Tugendhat: I do not know whether I misunderstood. Did you invoke the student satisfaction surveys as part of your evidence?

Lord Adonis: I was asked a question about whether students believed they were getting value for money. Lord Willetts was giving you figures for overall satisfaction levels, which is a different question.

Lord Tugendhat: I used to look at student surveys quite carefully when I was chancellor of the University of Bath. I should point out that that was some four years ago. At that time, I was interested in student satisfaction surveys and I was struck by the fact that, on the whole, the highest student satisfaction surveys were in campus universities rather than urban ones. One could quite understand why that was. They were able to enjoy the university and all the extracurricular facilities. Indeed, the University of Bath, which is a very fine one, has consistently had a higher student satisfaction rating than Imperial College, which probably rates more highly on the international scale. I am not quite sure how accurate a barometer the student satisfaction surveys are in measuring this particular point.

Lord Adonis: That is a fair point. The London institutions all score less highly. Lord Willetts will have more detail on this, but my understanding is that accommodation is a particular issue in London, because it tends to be more expensive and a lot of it is much more distant from the universities than it is in campus universities. That leads to high levels of dissatisfaction with the overall experience, even though the quality of the education is often higher.

Lord Willetts: I take this opportunity to agree with Lord Adonis. It is an example of how complex this is. I speak as a visiting professor at King's College London. He is absolutely right. It is an interesting example. There are higher levels of student dissatisfaction in London, probably associated with living costs and a weaker campus experience. However, employment and earnings do better.

One of the other factors as to why it is so difficult to set different fee levels is that universities located in parts of the country where pay is lower, on average, tend to have less well-paid graduates, because some graduates stay where they were educated. London has low satisfaction and high employment and earnings.

Lord Tugendhat: When one comes to employment and how much they earn and so forth within two, five or however many years out of university, what people read is more important in general terms than the university they went to. That is difficult to relate to the goal of the 2012 reforms.

Lord Willetts: I accept that point. The Vignoles-Shephard evidence is that, if you are looking at earnings, once you have allowed for social background and prior achievement, it is the course. Essentially, there is a group of high-earning courses: law, economics and management. There is a group of middle-earning courses, mainly STEM subjects. There are less well-paid graduates. The worst paid are in the performing arts. That is another reason why it proves very difficult to get into differential fees.

I do not know what conclusion we should draw from that. One conclusion would be that we should charge more for graduates doing courses with high pay, but sometimes, in the very same conversation, you are told that you should exempt all fees for students doing engineering. Do people really want to have higher fees for medicine? My view was that that was where there was a role for public policy and expenditure. The job of public expenditure is to compensate universities for high-cost subjects, but if we follow the logic of differential fees by graduate returns I think we would end up with results most people would be very uncomfortable with. In my experience, by and large, they do not want higher fees for doctors and engineers, and low fees for people doing history.

Lord Adonis: Tiered fees of that kind are precisely what the Australians have.

Lord Willetts: Yes, and it is not satisfactory. Australia is in a mess; it has static levels.

Lord Adonis: It has a three-tier system, which is related to cost but also to costs and returns. The highest tier is medicine, veterinary science and law, because they are both high-cost and high-return subjects. There is no perfect way of doing it, but that is one way of ensuring that there are differential fees.

Q4 **Baroness Bowles of Berkhamsted:** I think I am supposed to be asking about the purpose of university education. We have already explored that quite a lot, but I will persevere. Lord Willetts, you have already said that one of the purposes is managing the transition into adulthood and cultivating critical thinking, but that is not the only route by which people can do that. Probably, they develop an awful lot from 18 to 21. I have myself benefited from a university education and on-the-job professional education. Probably a lot of my critical thinking came more from that professional training than from university education. I also take up the point that our CEOs seem to be historians. Countries with higher productivity seem to have CEOs who are scientists and engineers, so I wonder whether there is a connection. We often hear from companies that the graduates they recruit are not job-ready. That begs the question: do we have the right approach in what we are looking for from university education? Is it delivering?

Lord Willetts: My instincts against central planning were very much confirmed by my experience as a higher education Minister. Routes into the labour market and subsequent careers are complicated, and the world changes fast. I remember a conversation with a young woman who had done theology at university and was making a very large amount of money designing Sharia-compliant financial instruments in the City. Who are we to say what will happen as a result of a university course?

Lord Lamont of Lerwick: There is a financial element in Sharia.

Lord Willetts: Correct. She was working in the City and applying her theological study. If we try to plan these things, we will miss the wonderful serendipity of how a modern, flexible, liberal society works. That is why I am with Lord Robbins on that.

On the wider question of job readiness, I have a sneaking regard for the former colleges of advanced technology, of which Bath is one, which have an extra year—the sandwich course—in business and practical employment. We should remember that, now, about half of all university students are doing vocational technical training courses that include time with an employer. They are getting qualifications to work as anything from a nurse to doing a real estate management course that the RICS has certified as suitable training to be a chartered surveyor. We could have taken a different route, but Britain has ended up with a large amount of our professional and technical education now happening in a university context, and that is why university students are absolutely entitled to know which of those routes lead to good, well-paid jobs.

Lord Layard: I should declare that I work in a university, and I know that the rate of return for university education is reasonable, but the rate of return for apprenticeship and further education is generally found to be a lot higher. Is it not peculiar that we have not put more resources and effort into developing that side of it? Instead, we adopted a 50% target, or whatever, and since then we have thought about meeting the demand for university places without creating enough attractive places for vocational education. Would you agree that our failure to develop the non-university vocational education route, both at lower and higher levels, is a major cause of the inequality of wages in our country? There are big structural issues, and it is wrong to be bullish about universities because they have to be set in the comparative context. What is being done about the alternative?

Lord Adonis: I strongly agree with what Lord Layard said. I do not think there is anything ordained about the fact that we have such a weak apprenticeship stream. I certainly do not think that, somehow, we have a weak apprenticeship stream because we have a strong graduate stream. We have a weak apprenticeship stream because the state has not devoted resources, energy and commitment to creating a strong apprenticeship stream. Many of the countries that have them also have very strong universities. It is not a question of regulation; it is a question of proper funding streams, proper qualification systems and a commitment by employers to foster skills among their workforce, which historically has not happened here.

The system from which I drew a lot of inspiration when I was schools Minister was the school system in Singapore. Singapore has a much lower proportion of students going to university than we have. Of course, it has an English education system by background. It had a choice 20 years ago as to whether it would significantly expand the number of graduates or the further education and apprenticeship route through what was called the Institute for Technical Education. When I was first writing about this for the *FT* 20 years ago, the Institute of Technical Education in Singapore was known by its acronym as It's the End, because, if you did not get to university and you went there, your job prospects were not good; you would be subject to all the vagaries of the employment market to which Lord Willetts has just referred. But the state reformed the ITE, and turned it into an outstanding world-class technical education college and linked it to apprenticeships. When you visit it now, it looks and feels like a university, but it is rigorously technical and is closely tied to apprenticeships. If we had given even one half of the attention to the reform and improvement of the apprenticeship route as we have given to the constant reforms of higher education funding and structure in this country over the last 30 years, I believe we would have had a world-class apprenticeship route.

Lord Willetts: I agree with a lot of that. Certainly, returns on level 3 and level 4 apprenticeships are high. The trouble is that too many of them are really below that educational standard. Just to strike a note of optimism, when colleges of advanced technology and polytechnics got university status, we did not bomb those institutions into oblivion. They still carry on. If one takes a step back, one finds that across the country there are universities with a range of different missions. If you set aside the debate as to whether they should be called universities, which I concluded was unproductive, and look at the University of Hertfordshire, you will find that it is delivering technical automotive engineering qualifications for people who then work in the automotive industry. If you go to South Bank, you will find that it is training people for advanced building trades.

Whether or not they are called universities, it is striking that these very similar institutions in places such as Germany and Singapore are themselves increasingly taking a university title; they are moving from being technical high schools to becoming technical universities. If we were to relax a bit, we could say there is a convergence. We do not need to strip the name "university" from South Bank or Hertfordshire. It is absolutely right that we should promote technical education; we find it in universities, and, by and large, around the world the places that do it well tend to seek university title in the end.

Lord Adonis: They do not charge their students £9,250 a year for doing their degrees across the whole of the system.

Lord Willetts: There is actually a higher public subsidy.

Paul Johnson: Lord Layard's point is completely right. We still do a very poor job for too many young people in vocational education. We need to focus more on apprenticeships. A serious issue is that Governments have tried, to some extent in the past, and have continually failed serially to make changes happen in an effective way. The serious question is why. Is it about political focus? Is it about resource? We certainly put a lot less resource into apprenticeships than we do into the university system.

In an economic sense, you could argue that what we have, for whatever historical reason, is a comparative advantage in doing more of this stuff through the university system than is done in Germany and some other countries. We should take that comparative advantage and think about ways of extending it, which was essentially what Lord Willetts was saying. You can talk about broadening the universities to do these technical things, but we do not have a funding system that allows it to happen in any other way, because there is nothing like that amount of resource and certainly nothing like that amount of structure around the alternative routes.

Lord Adonis: That has been true until now, but the introduction of the apprenticeship levy may be changing it. The single biggest infusion of funding into the education system at the moment is the apprenticeship levy. No one is quite sure what it is being spent on, and it may be the most important issue in education policy at the moment.

Paul Johnson: It is in danger of being like all the other things we have had in the system, like Train to Gain and so on, which is just a pile of money, free stuff and things being rebadged in order to get the money. I am not saying that is going to happen, but we have to be very careful that it does not.

Q5 **Baroness Harding of Winscombe:** Can I follow up on the naming convention that if we call everything "university" somehow it will work better? I would be interested in the views of all three witnesses on how we get more flexible university education, if you want to call it that because it feels better, with one year or two-year courses and courses you can dip into through a decade, not just three years. That seems to me, from a business perspective, to be a more effective means of building the skills we might need in the modern economy than assuming that all institutions doing three-year courses from the age of 18 to 21 is the right answer. What is your view?

Lord Adonis: The failure to offer two-year degrees is a serious one on the part of universities. One of the effects of stuffing their mouths with money, which is what we have done over the last five years, has been to reduce significantly the incentives on them to do so. The Minister for higher education, in what I think was a very surprising change in the rules, is now allowing universities to charge the equivalent of three years' worth of fees, taking out state loans over two years, as a way of encouraging them to offer two-year degrees when, surely, the rationale for two-year degrees ought to be that they should be at lower cost and at lower fees for the students.

My own view—maybe I am too much of a statist on these things—is that the Minister should have intervened and set requirements for the offering of two-year degrees, so that there is proper choice. Since there is a cartel operating in respect of fees, the very least the state could do is to see that real choice is offered to students, so that universities are able to offer courses for two years with lower fees than the three-year fees, not what the Government have said to universities, which is that they can charge the same.

If I can make another point about which I feel strongly, I have worked in many areas of the public service as a Minister and as a reformer, and there is none that uses its estate and assets less intensively than universities. For about a third of the year, the assets are significantly underused. When I suggested, and the heavens opened, a few months ago that maybe there could be a fourth term for universities over the summer—not that all students would be obliged to do four terms, although they could if they took a two-year degree—which would provide a great deal more flexibility and much more intensive use of the estate, many of my good friends, the vice-chancellors, said it was an outrageous suggestion, because they needed the whole of the summer to refurbish their science labs.

As a former transport Minister responsible for an underground system that is now the envy of the world and operates 24 hours a day for the best part of three days a week, and for 16 hours a day for the other four to five, that is not an argument I recognise. In this realm of very high fees, we need much greater efficiency from the universities and a much wider range of offers to students, including intensive two-year degrees. They are simply not on offer at the moment because universities are coining it from the existing fee regime.

Lord Turnbull: Lord Adonis, earlier in your evidence you said, apparently with approval, that lots of professional services companies are now putting their young employees through apprenticeships. I would have thought that was an abuse. Are they gaming the system? Is that what the apprenticeship scheme is meant to do? I thought it was an attempt to provide greater access to STEM subjects outside the university. I would argue that what we have instead is universities providing not STEM but sociology, tourism, entertainment and media, because those are the cheap subjects. Universities are incentivised to provide non-STEM subjects because they are cheaper, and we are not getting non-university young people the technological training they need, so both halves of the system are not working.

Lord Adonis: I do not agree that it is wrong for employers to offer high-level apprenticeship courses. I do not think that is an abuse at all. Indeed, they were doing it before the apprenticeship levy came in. The trend towards many more high-level apprenticeship schemes goes back four or five years. It is a response to the demands and preferences of young people, and employers' own operation in the labour market, to make offers attractive to young people too.

I do, however, think it was a very serious mistake—I would never have done it as Minister—to rebadge all the polytechnics as universities in 1992. It was a reform done without any proper consideration or advice; it was simply announced by the Government. I was education correspondent of the *Financial Times* at the time and I remember that it was announced over one weekend. We have lost a great deal of the edge and focus of vocational, particularly technical, higher education as a result. There is a very good case for reversing that reform in respect of the lower-performing former polytechnics, in the context of a very significant reduction in the fees they are allowed to charge to students, so that we can offer a much better deal to students as part of a new reform.

Paul Johnson: I have two points in response to that question. First, it appears that for universities there is an incentive in the system to provide lower-priced courses, such as the arts. Actually in the numbers, those for STEM courses have gone up relative to arts courses since 2012. Whatever the apparent incentive, perhaps because the demand from students has changed, it has not, as far as we can see, been played out.

The second point, on apprenticeships, is that it worries me when we talk about apprenticeships for fast-stream civil servants and accountants in the big four accountancy firms, which is just another route for the really high-attaining kids with A* A-levels. The real problem is not for them at all. If we are talking about apprenticeships, we should at least in part be talking about the appropriate route for those who are not doing brilliantly in their A-levels. It is a mistake to think about that sort of route as the apprenticeship route.

Baroness Kingsmill: In a company in Germany, on whose board I sit, we have a very highly developed apprenticeship scheme, and it is not an either/or graduates or apprenticeships. We have five-year apprenticeships for non-graduates and three-year ones for graduates. It is exactly the same apprenticeship; it is just that it takes one lot five years to do it and the other three years to do it because they have a degree. The status attached to both is exactly the same.

Lord Adonis: I strongly disagree with what Paul Johnson has just said. Only when apprenticeships become a high-status route will they become a route that a lot of lower performers, as well as high performers, go down. We should celebrate the fact that many alternative routes to graduate degree courses have been provided by apprenticeships. We should not criticise that and say that it is a retrograde step.

Paul Johnson: I agree, but my point is that the specifics in this discussion have all been about that group. It is important to be clear that that may be part of it, but it is not the key problem. The problem with the UK system is not that we have a problem for the kids who are getting three A* A-levels.

Lord Willetts: May I respond to what Lord Turnbull said? This is very important. We want high-quality technical education. If you go to the University of Coventry and see the way it has structured its automotive engineering programme to link into the needs of Midlands industry, and similarly go to Teesside and Sunderland Universities, you see it happening. Lord Adonis said that the underperforming universities had to be stripped of their title and take on this role. We should do what is done in the US. People do not sit around in the US agonising that they have institutions called universities that are training people to work in a General Motors car plant in the middle of states. They accept that that is one of the things a university does. It does not make it a bad university; it makes it a different university from a Newman/Oxbridge university, but it is a legitimate function. Even in Germany, they are increasingly giving university title to the institutions that do that.

Lord Adonis: I come back to the central point that under our fees cartel those institutions are still charging students £9,250, so there is no differentiation between them.

Q6 **Lord Layard:** I want to note that all the time we keep coming back to the top 50%. I want to go back to the question I raised, which is not about the top 50% and the subtleties of exactly what kind of route they take, which is important, but the other 50%. None of you answered my question. Do you believe that our neglect of the education of the other 50% is a major reason why we have a more unequal wage structure than any other European country?

Lord Adonis: Yes, I do. If you look at the level of investment in those who do and do not go through higher education routes it is very stark, so I completely agree with that.

Lord Willetts: I accept that. The paradox of our financing changes is that, because they took higher education out of public funding, that releases public funding for areas that clearly are in much greater need of public subsidy. It seems to me reasonable that, if you have a bit of education that clearly links to high wages afterwards, you can expect the people in higher-paid work to pay back, so you use your limited public resource for things such as the priorities you are describing.

Paul Johnson: David is slightly having his cake and eating it by saying it has taken the universities out of public funding. It has not; it has just delayed the point in the national accounts at which public funding kicks in. There is at least less of it than before, but there is still a lot of public funding there.

The Chairman: Too many cakes.

Q7 **Lord Burns:** Do you think the changes recently announced by the Prime Minister will make any significant differences to the system?

Lord Adonis: They will add quite a lot to the costs, but they are not going to make it more publicly acceptable, and at the moment it looks to me as if the whole system is a pack of cards waiting to collapse. It reminds me of the poll tax. Each bolted-on reform to try to make it more acceptable simply added to the costs, made it more baroque and hastened the day when the whole system collapsed. Now the Government have said that the whole system is under review.

The bit that is most objected to by students is the 6.1% rate of interest; a university education has moved from the best deal you can get on a loan to the worst deal. That is very expensive to put right. It will cost many billions to reduce that 6.1% because it applies to the generality of the loan, not just the fee loan but the living cost loan as well. At the point when the Government change that rate, which they will be obliged to do before the next election—I cannot see them going into the next election with 6.1%—the financial model collapses. David was telling us that it was great that the number controls had been removed. All those will come back again because there is no way the Treasury will take on those costs without regulating the numbers much more rigorously than it does at the moment.

My view is that the state will then move in a serious way to start reducing the actual costs of courses, too. David was saying earlier that we should be spending more in order to make university education akin to a secondary school. The unit of resource for a secondary school in England is £4,800, which is almost precisely half what we pay for university courses, many of which are considerably less intensive than secondary school courses. Just the comparison of those two figures, which our colleagues in the Treasury are well aware of, will make the existing system unsustainable at the point at which the state has to take on more of the costs.

Paul Johnson: In answer to the question and the comment about interest rates, one issue is about quantum. Once you have the quantum, the issue is essentially about redistribution and how you pay for it. The actual increase that the Prime Minister announced in the point at which people start to repay fees was a much bigger change than it looked. It makes a significant difference to the cost of the system, increasing it significantly in the long run. It reduces significantly the amount that students pay, and particularly significantly reduces it for lower and middle-earning graduates.

The issue about the interest rate is interesting. It is essentially a question about redistribution within the system. If there is a high interest rate, the effective result is that quite high earners will pay back significantly more. It makes no difference at all to the amount middle earners pay back. There is clearly a perception issue, but, in reality, the choices about interest rates and the point at which you start to pay back are about distribution in the system and the extent to which it is providing, within a set of resources, insurance for graduates and creating redistribution from high to low earners. The risk with a high interest rate—you might not see it as a risk if you are sitting in the Treasury—is that those who are confident they will earn a lot will pay back early. If I was sitting in the Treasury, I would probably be quite happy about that, even if it meant that there was a group of very high earners who paid back a bit less than the moderately high earners.

Lord Burns: Does that not show some of the many dangers of the scheme and the problem about what it is called? We have a loan system that David keeps telling me is not really a loan system but a contingent-income system. We have an interest rate that people see, and they notice that after they have paid back their loan remains exactly the same as it was before. They do not understand the extent to which it is all tied up with redistribution and have no idea where the cost is falling. Is not a fundamental problem with the scheme that it does not remotely do what it says on the tin? The components of it are so desperately complicated that people cannot tell what impact it will have on them.

Lord Willetts: For a graduate it is very simple; it was 9% of your earnings above £21,000 and now 9% of your earnings above £25,000. I agree it is a great pity that we got trapped in the language of fees and loans. Vince Cable and I looked at whether we could escape from that. Our conclusion was that it was already so embedded that, although it was a misnomer, and it was not an overdraft or credit card debt, we were trapped in that language. It is a graduate repayment scheme.

One thing I would add to what Paul Johnson said is that occasionally people say, "We now know that 83% of graduates will not be repaying". The repayment terms are a legitimate political and social decision. Essentially, it is a decision about how far the generality of taxpayers meet the costs of less well-paid graduates and the extent to which graduates pay back. I personally think it was not necessary to go from £21,000 to £25,000, but the forecast of the so-called RAB charge assumes that everything is fixed for the next 30 years.

Of course, the scheme has to be recalibrated. It has just been recalibrated in rather tough political circumstances. If the Committee thinks graduates are not paying back enough, it could say that the repayment terms should change; it should go back to £21,000 or, as under Labour's scheme, £15,000. If 9% is too high, you could reduce it. If you are worried about marginal rates in the labour market, reduce it to 6%. That is how it should function. What I have long called for is a review once a Parliament of the features of the scheme, so that we keep the basic principle of graduate repayment but adjust it to whatever you think is a fair balance between graduates repaying and the generality of taxpayers writing it off.

Lord Burns: If you pursue that route, do you not agree that things like a 6.1% interest rate complicate and obfuscate it for many people, which means that they cannot really understand it?

Lord Willetts: It was brought in to make it more progressive, and you can get rid of it.

Lord Adonis: But it constantly changes.

Lord Willetts: It was brought in to get higher repayments from well-paid graduates. That was its purpose. I realise it is controversial, and I personally think that is the pressure point politically, not the repayment threshold of £21,000 or £25,000.

Lord Burns: You may say that was why it was brought in, but I do not think that is remotely clear to the people on whom it falls.

Lord Willetts: That is a fair point; I accept that.

Lord Adonis: David just said it should be reviewed once a Parliament. There is a review once every six months at the moment. The Prime Minister announced fundamental changes, costing huge sums of money, in a speech last week, and that is before the review, which may recommend more fundamental changes. This is more and more like the poll tax. The only constant is that, with each reform, the costs go up. The costs to the Treasury go up. A scheme that was supposed to relieve the Treasury of money is able to do so only by funny accounting mechanisms that get the whole lot off the balance sheet at the moment, but when it starts to come back, as it will do, the pack of cards will collapse.

One thing that ought to be of very great concern to the Committee, as it is to me, is the constant retrospective changing in the rules in respect of students and graduates themselves, which I think is deeply unfair. The student and the graduate are, effectively, entering into a contract with the state when they agree to take on a course. What is happening at the moment is that, literally every year, the state changes the terms, to their significant disadvantage.

Lord Burns: Not this time.

Lord Adonis: This one is to their advantage, but until now they have all been to their significant disadvantage, and I do not think that should be acceptable.

Q8 **Baroness Bowles of Berkhamsted:** Given the changes that have had to be made in order to make the adjustments you have just discussed, in retrospect what makes it better than a graduate tax scheme?

Lord Adonis: You cannot do a straight graduate tax. We looked at it seriously in 2004, and I understand that David looked at it before. There are so many reasons why it will not work. One of them is that, as soon as you make somebody liable to a rate of tax for being a graduate, you have to define what being a graduate is. That is a very difficult task. As soon as you have to define a graduate for the purposes of paying a lifetime tax, which is a very big burden, you suddenly discover that two-year diplomas, or indeed 11-month and 60-day diplomas, which are not quite degrees, become extremely fashionable, particularly in universities that may even name themselves non-universities in order to avoid the tax. It is impossible as soon as you start. It sounds great. It is a very glib answer and it is totally unworkable.

Lord Willetts: Something else on which I completely agree with Lord Adonis.

Lord Adonis: The higher rate of tax is effectively a graduate tax. Only 17% of taxpayers pay the 40p rate, and almost all of them are now graduates. If you wanted to have a tax that is essentially a tax on graduates, increasing the 40p rate would be equivalent to doing so.

Q9 **Lord Turnbull:** Earlier, one of you said that the interest rate was increased to make it more progressive. I would suggest it was done, like lots of other features of the scheme, to flatter in the short term the public accounts. The higher the interest rate, the more the revenues of the state go up and the smaller the deficit. The write-offs come many years later, so it makes the reduction in the deficit look better than it really is. It has been described by the OBR as a fiscal illusion. I suspect that the shift from maintenance grants to loans was done for exactly the same reason, because the loans do not appear on the public accounts until much later on. Do you think that the Treasury obsession with the deficit is forcing non-optimal decisions?

Paul Johnson: I cannot comment on what drove it. You are absolutely right. It is a slightly odd situation in which money that we pay out at the moment does not appear on the borrowing numbers but does appear on the debt numbers. There is a very odd effect from the interest rate. A bizarre impact of the increase in the repayment point from £21,000 to £25,000 is that it makes the public finances better in the short run because more interest has accrued before you start paying it back. In any sense of controlling the public finances that is clearly an absurd way of looking at it, and it is one of the many ways in which the public finances ought to be looked at to consider the long-term impacts of this. Clearly, the change improved the public finances in the long run, because money would be paid back in the end. Where we have got to now is that it probably has not had much impact on the book finances, even in the long run, with the increase in the point at which you pay back, alongside the fact that graduate earnings have turned out to be so much worse than previously expected. There is real change. There is real additional revenue for universities at, in the end, no additional cost to the taxpayer, but significant individual cost to the graduate. Real change is there, but unquestionably it significantly flatters the public finances in the short run, relative to the reality.

Lord Willetts: The way in which interest rates affect the PSBR could be the reason why, when the politics at the moment is around interest rates, we have not had a move on interest rates, which would have been the obvious thing to do.

More widely, there is a set of public financing rules, independently set and assessed. The underlying issue is quite simply whether we think graduate repayment is a fair way of financing higher education, setting aside exactly how it is treated in the public finances. There is a large body of economic literature, and several advanced western countries around the world, saying that, given that on average graduates earn more, expecting them to pay back, rather than the generality of taxpayers who will be less affluent, is a fair and progressive way of doing it. I am up for adjustments and so on, but my view is that universities suffered when they were just another claim on the Exchequer, and we did not expect graduates to make a contribution. There is still a big prize. Expecting graduates in well-paid jobs to pay back the cost of their higher education, and in return giving greater freedom to universities to compete for those graduates, is the underlying deal, and it is what I believe in.

The Chairman: Are you saying it is a good idea but the execution has not worked out well?

Lord Willetts: When you get into the details of whether the interest rate counts towards the PSBR, Paul and Lord Turnbull are absolutely correct; it is an odd effect and the OBR quote is a telling one. I am trying to take a step back from that. My worry is that we lose the big prize, which is a graduate repayment scheme, with universities competing for students.

The Chairman: That is not Lord Turnbull's question.

Lord Turnbull: The 6%, much of which will not be paid, has turned the public against the scheme and we have lost the basic principle, which is absolutely right. Greed to squeeze the maximum out of it is casting doubt on the whole thing, and we may end up with the thing collapsing and having something worse.

Lord Willetts: There is no reason why it should collapse. I find it hard to see any Treasury that would wish to see it brought back on to public spending. The interest rate is absolutely not a core feature of the scheme. I cannot divulge the coalition discussions, but it was put in mainly to make it more progressive. Honestly.

Lord Adonis: I am not sure which planet David lives on. He says there is no reason why it should collapse. One of the major political parties in the last election proposed to scrap the scheme entirely. The other one has already scrapped part of it, and has now announced a fundamental review of it, which will almost certainly add significantly to the costs and make it unsustainable, and we have a revolt taking place on campuses by students who simply do not believe they are getting value for £9,250 plus 6.1% interest. At the moment, the scheme has death written all over it, so the idea that it is going to survive another four or five years is unsustainable.

If I may add a bit of international context, the trend internationally is towards abolishing high levels of tuition fees. We went through a phase of introducing them. They got out of hand in the United States where they are being progressively abolished by state governments; Germany introduced fees and they have almost universally been abolished; and Australia has them under much greater control. The mistake that David made in trebling the fees overnight has essentially destroyed the system; and a very good principle, which many of us fought hard for, to have co-payment between students and the state, has been completely undermined by moving the entirety of the cost from the state.

The Chairman: Can we focus on Lord Turnbull's question, which was about the fiscal illusion? It seems rather odd that the interest payments being made at 6% as soon as the student arrives at the institution are treated as income, when the changes mean that 83% of the money will not be paid back, but it does have the effect of flattering the reduction in the deficit by £5 billion or £6 billion. Was this done as a way of tackling the numbers in the deficit, or was it done, as Lord Willetts suggested, as a way of further cranking the redistributive effect of the scheme? Can you answer that question, Paul Johnson?

Paul Johnson: It has both effects. I could not speculate on how they were weighed up when Ministers were taking their decisions.

Lord Willetts: I was in the room at the time. I can tell you that there was pressure from our coalition colleagues to make this as progressive as possible. The inhibition on the Treasury, given the politics around the interest rate, and the fact that it has this PSBR effect, may be one of the reasons why we have ended up with the repayment threshold changing—not the interest rate—but neither the exact level of the repayment nor whether or not there is an interest rate is a fundamental feature of the scheme. I have a recollection of the days when the media stories were about affluent students collecting their full maintenance loans, investing them in an ISA, making some money on 0% interest and making a profit at the end. The dynamic of these things changes and the system should change, but it would be a great pity if we went back to a system where this was public expenditure and rationed as such. That would not be in the interests of students or universities.

The Chairman: Lord Turnbull, are you happy with the answer?

Lord Turnbull: It may be this interest rate is in two halves. There is a 3% inflation rate and then there is the real interest rate. Nowhere is it said that the real interest rate should be charged at 3%. It is not the real interest rate on indexed gilts; it is not what you can earn anywhere else. I just do not understand how this number could possibly be justified.

Paul Johnson: It depends on what you are trying to achieve. As David said, if you are trying to achieve progressivity within the system, that is a way of doing it. Given where we are, the move to a higher repayment threshold was a more progressive change than a change to a lower interest rate. Of course, the actual number is plucked out of the air and as an interest rate it makes no sense, but for the vast majority of graduates it does not make any difference to how much they end up paying. Without question, there is a problem of perception, but the amount they actually end up paying is a way of introducing within this thing called a loan system a degree of progressivity.

Lord Adonis: This is like one of those cathedrals that every century has another wing added to it. There is a new flying buttress because one bit is threatened with collapse. Then the bell tower falls down and has to be completely rebuilt. That is the state the student finance system is in at the moment. The idea that it is sustainable is so far removed from both the financial and political realities that it is a farcical proposition. The only question is when it collapses—whether it is this year, next year or at the next election. I hope that the Committee puts in place a more robust system to replace it before the really serious thing happens, which is that we leave the universities penniless.

The Chairman: You have made that point repeatedly. Paul Johnson, in answer to my previous question, you said that both things applied. The fact that the interest rate was increased, which had the effect of making the deficit reduction look better according to Treasury rules, and the fact that it was combined with changing the discount rate suggests that perhaps there was a motive to make the thing fit within the criteria, or am I just being cynical?

Paul Johnson: It would not surprise me if that was part of the motive, but I really cannot comment on it.

The Chairman: Lord Willetts, you were in the room. What do you think about that?

Lord Willetts: I found the RAB charge the most absurd part of the theology of the graduate repayment scheme. It has implicitly been referred to several times today. It is an attempt to forecast repayments over the next 30 years in a system for which you have to make assumptions about earnings, about the repayment threshold relative to earnings and about rates. It has had far too much attention. It has very limited value, and, as I said, my view is that every few years we should review it. The fundamental issue about the discount rate was that the Government were choosing one that made the RAB charge look even worse and that, it could be argued, was implausibly high because it was significantly higher than its actual cost of borrowing. That was why my successors brought down the figure used for that.

On the repayment threshold, when I set it at £21,000, it was done on the basis that we expected earnings to be higher by 2016 than turned out. As earnings underperformed, the repayment threshold got higher relative to earnings. Every six months from 2012 to 2016, when the new earnings figures came out and showed earnings were not growing so much, the

RAB charge went up, because the new higher level of the threshold relative to earnings was then assumed to last for the next 30 years. That kind of thing is very persuasive. If the repayment threshold ends up being a bit more generous than we expected, the reasonable thing is to freeze it, which is what my successors did, and the RAB charge started going down. These things are all manageable as legitimate public policy decisions.

Lord Layard: Do you have a suggestion on how to handle the problem of perceptions, because it is absolutely right that the thing is being destroyed by perceptions?

Lord Adonis: I think it has gone beyond the point at which you can manage the perception.

Lord Layard: I know you think that.

Q10 **Baroness Kingsmill:** To add a bit more controversy to the discussion, what about the idea of selling the loan book? What are your views about that?

Lord Adonis: I think Lord Willetts was in the room for that one, too.

Lord Willetts: This is not an oral history unit.

Baroness Kingsmill: In any event, how would it help the big picture to which you have referred?

Lord Willetts: It is not unlike the interest rate discussion we have just had. It is the case that within the rules of accounting, which are set by outside bodies, the doctrine is that the Government have a liability when they provide the loans, and that liability adds to the national debt. However, the asset, the repayment of the loans, is not regarded as sufficiently liquid to be an asset that offsets the liability, so the asset does not affect the national debt. I am looking to Paul Johnson to check whether I have put it correctly. That has the result that, if you sell the loan book as an asset sale, the cash proceeds from that asset sale reduce the national debt. If you are sitting in the Treasury and you have a national debt target, selling the loan book is a means of reducing the national debt. That is the financial engineering side.

For me, is it worth doing? I personally would do it only if you could use it to create an incentive for universities to engage with the performance of their graduates out in the labour market, and themselves see higher repayments as a result of further investment in their graduates. I have tried to explain neutrally the financial accounting treatment of it.

Paul Johnson: It is hard to see any good reason for selling the loan book. The basis on which it was sold would still mean that the state, through PAYE, was collecting the money. There is no sense that you would sell it off and then the private sector would collect the money, so the only thing you would be doing would be a financial transaction. The cost of finance in the private sector at the moment is significantly higher than in the public sector, so in the long run the public sector surely must lose out. The only reason for doing it would be for short-run financial engineering reasons. I cannot see any reason for selling it.

Baroness Kingsmill: Lord Adonis, do you have a view?

Lord Adonis: It is all smoke and mirrors, is it not? The substance is what matters. The substance as regards the repayments to which graduates are liable would not change at all, so, as Paul says, as a financial transaction it is neither here nor there.

Baroness Kingsmill: How much money are you going to get when there is non-repayment of 83%?

Paul Johnson: There is not non-repayment of 83%. About 80% would not pay it all back in full. The numbers have changed in the last week or two, but it might now be about 60%, depending on the discount rate and so on.

Perhaps you think the private sector is more able to bear the risk, but the idea that it is more able to bear the risk of uncertain repayment seems a little odd. There is very little rational reason for doing it other than the financial accounting reasons that David completely correctly described, which are a pressure on the Treasury.

Baroness Bowles of Berkhamsted: On the issue of illiquidity, and not being able to count it as an asset in the national system of accounting, does that derive directly from the international requirements as to how you specify debt? It is not something we could change.

Paul Johnson: In all these things, happily in many ways, we cannot bend the rules ourselves. Some of the rules are silly, like those on interest rates and so on, but they are not ones that the Treasury particularly can change; it is rather important that it cannot.

The Chairman: When the Chancellor gave evidence to us at the beginning of last month, he was asked about why he might sell off the loan book. He said, "It is the Government's intention, where they find that they hold assets on the public balance sheet for which there is no policy or strategic reason, to realise those assets and thus reduce public sector debt, helping us to achieve our debt targets and/or create capacity to do other things in line with policy priorities".

Paul Johnson: It is hard to know why in any rational world it would give you more space. It would, if anything, reduce the public sector net worth and not increase it, given that the value of this thing is probably lower in the private sector than in the public sector.

The Chairman: But there is a short-term benefit.

Paul Johnson: There is a short-term benefit to the measured financial debt, but that is an illusion created by the slightly odd way in which we look at the public finances.

The Chairman: Do you detect a pattern there?

Paul Johnson: Most of these things move in the same helpful direction of short-term public finances at the expense of the long-term public finances.

Lord Willetts: There is a pattern. Let me level with the Committee on how I think it worked. If higher education is public spending, it is at the bottom of the queue. That is the evidence from the last 25 years. That is why the unit of resource for students was falling; that is why the so-called stuffing their mouths with gold was just catching up with much higher rates of education spending in other parts, such as secondary and primary education. The view of successive Governments has been that higher education loses out in the public sector.

However, equally, we do not want an American commercial loan system. You are regulated as if it is a commercial loan; you immediately have to know your customer and you have to decide whether to lend to Janet or John. Janet comes from a poor home and she will not earn so much, so you will not lend to her. You choose to whom you lend.

The aim is a graduate repayment scheme that is neither public spending nor a commercial loan scheme. The reason why we have ended up with this, setting aside all the baroque complexities around the edges, is that we are trying to do something that is a universal scheme for all students and is not a commercial loan and is not public spending. That is the core decision. My view is that that remains the correct strategy for financing higher education in England. Almost everything else is negotiable and adjustable, but if we gave up on that we would be in one of the other two scenarios, and either horn of that dilemma is worse than where we are now.

Lord Adonis: The extraordinary thing about what has happened with all these changes is that, despite what David has just said, we have ended up with something that is worse than a commercial loan, because 6.1% interest is now applied to it, unless you are lucky enough not to have to repay it. If you have to repay it, the terms on which you take on the loan are worse with 6.1% interest than they would be if you had a high street loan at the moment.

Baroness Bowles of Berkhamsted: What is to stop the better off students having a commercial loan?

Lord Adonis: That might well be, or if you come from a well-off family you are much better off with your parents paying off the loan, which is what will increasingly happen.

Paul Johnson: I have to disagree with Andrew in the way he has described the system. This is not in any sense worse than a commercial loan for at least 90% of students, in particular those who are going to have less than stellar earnings as they go into the labour market. There is no risk associated with this that you will be chased in 10, 20, 30 or 50 years' time for not repaying it. As David said, it is an income-contingent loan that looks to anyone paying it very much like a tax payment.

The Chairman: But the point made by Baroness Bowles, as I understood it, is that if you are a student who ends up earning a lot of money, or has wealthy parents, the terms of repayment are considerably worse.

Paul Johnson: That is clearly true.

Baroness Bowles of Berkhamsted: They might just opt out.

Paul Johnson: They might, and some do.

Baroness Bowles of Berkhamsted: And you do not get your money back from the ones who do not pay.

Paul Johnson: Yes, and that is part of what makes it progressive.

Lord Adonis: What Paul is saying is that for some it is not worse. For many it is worse, which is the reason why they will choose to pay it back, because 6.1% interest is much worse than you can get by way of a loan. If you have a reasonable assurance that you will be a reasonably high earner, the risks he has mentioned would not apply anyway. The crucial inequity is that, if you are lucky enough to have wealthy parents, they will simply write off all the debt for you. They will obviously do that rather than saddling you with 6.1% interest knowing that you will have to repay it because you will get a reasonably secure job.

What began as a system intended to be non-commercial has in fact become thoroughly commercial. Some of those who are lower earners will benefit from some of the terms of the loans, but those who do not will end up paying a great deal more than they would have done.

Lord Willetts: It is not a commercial loan scheme. That is not a useful comparison to make; it is completely different.

Q11 **Baroness Harding of Winscombe:** Lord Adonis, you have been very clear about your dislike of the design of the current system. How feasible is it to abolish tuition fees entirely, and what is your alternative to the system we have?

Lord Adonis: The reason why I have been so firm on this is that what I think was a very worthwhile reform, which would have meant a reasonable contribution on the part of students and, by international standards, was fairly mainstream in the way policy was going 15 years ago, representing roughly half the cost of a typical degree, which is what we were aiming for when we introduced the £3,000 fee regime, and was justified as a system of co-payment, has been turned by a series of very misguided reforms into a system that is politically unsustainable, because it shifts most of the cost of higher education teaching to students. Indeed, for a significant proportion of students, it requires them to pay significantly more than the actual cost at the moment, and significantly more than the cost if there was proper cost control on universities, which have had no incentive to bring down their costs, because they have had a windfall.

Baroness Harding of Winscombe: Looking forward, rather than critiquing again what we have got, is it feasible to abolish tuition fees, and what would you do if you cannot?

Lord Adonis: I would love to be able to go back to the system before David ruined it, but that may not be possible because of what has happened.

Baroness Harding of Winscombe: For the reasons that have been set out.

Lord Adonis: If it is not possible to do that, what will happen is what is happening across the United States at the moment and has happened in Germany. I think it will happen in Australia and New Zealand in due course, too. The fees and loan system will be scrapped outright, and instead there will be a trade-off with higher top rates of tax, which are essentially paid by graduates. To my mind, that is not such a good arrangement for universities, for a reason on which we and probably most members of the Committee would agree: having an independent income stream for universities is a worthwhile thing. But the system has become so discredited in the minds of graduates and the public at large that it will be very hard to put Humpty Dumpty back together again.

Lord Willetts: Perhaps I might make a couple of quick points.

The Chairman: I think you should be allowed to.

Lord Willetts: Lord Adonis says "discredited". Actually, university students have more resource behind their education than ever before. Compared with the £3,000 fees that we inherited, there were two big changes we made that we saw as improvements. First, when there was a very large amount of public expenditure grant as well, there were number controls as a way of controlling the size of the grant. As late as 2012 or 2013, each university was given a number—set centrally—for the number of students it could recruit. I saw getting rid of that as a big prize.

Secondly, the repayment threshold in the old system was £15,000. If Lord Adonis is so worried about graduate burdens, the fact is that 9% on your earnings above £15,000 is a hell of a sight more onerous than 9% on your earnings above £21,000. Having got very interested in intergenerational equity, I was particularly worried about the burden on people in their 20s and 30s. Essentially, the repayment was front-end loaded. You paid back a lot through your 20s and 30s and then it came to an end. I took the view that it was better if it was not front-end loaded, and you paid back more but for longer. That is why I am not so troubled by the argument about many people not paying it back in full. I did not want people paying 9% on earnings above £15,000; I thought it was tough on them as they were getting started on the housing ladder, so I wanted to lower the fixed outgoing a graduate faced; £21,000 did that. There were no number controls and a lowering of the fixed outgoing.

Q12 **Lord Layard:** Paul Johnson, you have proposed making a gift of £10,000 to every young person on reaching their 21st birthday, as an alternative to abolishing tuition fees. How do you think that would work, and how would it be afforded?

Paul Johnson: It was not so much a proposal as a way of putting the issues in sharp relief. People give two reasons for wanting to get rid of tuition fees. One is that they are a particular burden on the younger generation, and it would in some senses be progressive or helpful to move away from tuition fees. The point of putting that out as something against which to make a comparison was to say that, if you were to abolish tuition fees, clearly the biggest gainers in the long run would be the highest-earning graduates; other graduates would be moderate gainers, and the half of the population who do not go to university would gain nothing.

Lord Willetts: They would pay taxes instead.

Paul Johnson: If your concern is about intergenerational equity, for less than the cost of abolishing tuition fees, you could give, at age 21, 25 or whatever, £10,000 to all young people. If the reason for your concern is one of intergenerational equity, getting rid of tuition fees is possibly the worst and least progressive way of doing it. There might be all sorts of other reasons for wanting to get rid of tuition fees—because the market is not working, universities are misbehaving or all those sorts of reasons—but if the issue is one of intergenerational equity, there are better ways of achieving with a smaller amount of money a much bigger gain. That was the intellectual point I was trying to make.

Lord Layard: On perception, going back to the question that the other two witnesses did not answer, £10,000 is a bit less than a debt of £65,000, so it does not seem to deal with the problem for that group of people. I can see a lot of arguments for equal resources for everybody for post-school education. That is a different thing, but I do not quite see how it deals with the presentational issue.

Paul Johnson: It does not. The proposition was not that it would deal with that presentational issue. Intellectually, the proposition was that, if you are interested, in a progressive way, in doing something intergenerationally helpful to the younger generation, spending a certain amount of money on a £10,000 demogrant is a more equitable way of doing it than getting rid of tuition fees. That is the point I was trying to make.

Lord Sharkey: But it is not in practice scalable to solve the problem we are trying to address.

Paul Johnson: I am not suggesting that it would be. All I am saying is that if your issue is one of intergenerational equity—a number of commentators say that the key point is that the current generation of young people is doing really badly, which it is, relative to previous generations—and you want to solve that problem, a very bad way of doing it for the generation as a whole, certainly in a progressive way, would be to get rid of tuition fees, and a much better way would be to give a demogrant. There are all sorts of other problems with the funding of universities, the structure of tuition fees and so on that that would not address at all, and it was not intended to. If you are worried about intergenerational equity, that would be a better tool, if you had the £8 billion or so that it would cost.

The Chairman: It is an eye-catching initiative.

Paul Johnson: We have one eye-catching initiative coming from one of the main parties, which is to abolish tuition fees at a cost of £10 billion or £12 billion a year. For about half of that, you could give everyone 10 grand.

Lord Adonis: I think the 6.1% rate of interest was pretty eye-catching as well. They notice that, too.

Q13 **Lord Sharkey:** If you could make one change to the current ruined system of education policy, what would it be? Perhaps Lord Willetts, not Lord Adonis, could go first.

Lord Willetts: Following on from the previous intervention, if someone said, "I want to put more public spending into higher education", it would not be a priority to have a general replacement of fees and loans by going back to the days of grants. There are specific things one should do. My personal shopping list, as came up earlier, would be to do something for mature part-time students. The loss of a means-tested maintenance grant is a pressure point for low-income students. I am not sure that the costs of high-cost subjects, such as engineering courses and things like that, are properly met at the moment, so if we want universities to teach engineering with up-to-date kit, we should put money into high-cost subjects. You could spend a billion or two on some quite effective changes.

More widely, the fundamental problem in our higher education system is the way we specialise at the age of 16. In that respect, the Scottish system is far better. A lot of the problems we face—on students doing STEM, for example—arise from the decisions we expect 16 year-olds to make, which almost every other country expects 20 year-olds to make. The deal is that we specialise early and get people through education quickly. That is why I did not completely agree with the two-year course. We have some of the western world's youngest graduates. We could have a broader education for longer, perhaps even a four-year university course. I always thought that that would be the next stage of the reforms I brought in. I thought that, once we got it out of public spending, we would be able to have a shift to four-year courses. The Robbins vision and the Keele-Sussex idea of a broader education collapsed because the Treasury would not fund four-year university courses. I thought that would be the next stage of education reform.

Paul Johnson: I agree with a lot of that. I would like us to stop obsessing about higher education finance and the way it is done at the moment. If we have a series of problems with our education system, it is not the higher education finance system. It might be in perception terms, but objectively it is not. We have much bigger problems with the breadth of our education, our vocational education systems and the length and depth of some higher education courses. I would stop obsessing about it and spending so much time in the public domain worrying about the precise way in which we pay for universities, and spend a lot more time wondering why we have incredibly specialised A-levels and why we make it incredibly difficult for kids who are not going on to university to find their way through the system.

I agree with some of Andrew's worries about the way the higher education system works at the moment, because clearly it is not working effectively as a market. There is a lot of money, both public and graduate money, going into it. If we are to have a review of the system, we should think really hard about how we regulate it in a way that will provide value for money. For the reasons we have discussed, we do not have a price-sensitive market. Universities have a lot of freedom, which is positive, but students have difficult choices.

Clearly, universities are getting more for some courses than the cost of delivering them and there is considerable variation in quality. What is the right regulatory structure? In other areas of the private sector, whether it be water, electricity, telecoms or whatever, if there are market problems and there is no effective competition, we have more or less effective economic regulators. I do not know what the outcome would be and how you would do it, but there is a case for a serious review of how you regulate this sector.

Lord Adonis: The Government have just completely changed the whole regulatory system, so the idea of another change on top of that is not very appealing.

In answer to Lord Sharkey's question, in my view the single biggest failure of the English education system since the Second World War was the fact that the technical schools promised in the Butler Act never materialised. It was that that discredited the system and prevented us taking the course that the Germans took. There is nothing ordained and cultural about this. The reason why we did not have a German quality secondary education system is that we had grammar schools without technical schools. The Germans had grammar schools and technical schools. Instead, we had grammar schools and secondary moderns.

Secondary moderns were essentially warehouses for secondary age pupils with no qualifications. There was no system of qualifications at all in secondary modern schools until the 1960s, and when they were introduced they were substandard. There was no investment in technical education, and no organised pathway into apprenticeships or further education beyond 16. That produced a big revolt against the secondary modern system, which was essentially what happened in the 1960s and

1970s. That resulted in the move towards comprehensives, which unfortunately had the effect of significantly segmenting and reinforcing the elitism of our system, because it pushed a lot of grammar schools into the private sector. We have the largest private education sector in the western world by an act of government policy in the 1960s and 1970s, without putting right the technical education issue at secondary school. If we had got that right, the follow-through in further and higher education—producing more engineers, technicians and so on—would also have been put right.

I would love to be able to turn back the clock to 1944 and put that one right. We cannot do that, but what we can and should do is to put a much higher premium on technical, secondary and further and higher education. Unfortunately, most of the reforms that, frankly, have happened under Governments of both parties in the last generation have not had that effect. Until we tackle that problem, we will still be at a very significant economic disadvantage compared with the countries in the world that have the best education systems.

The Chairman: That concludes our session. I thank Lord Willetts, Lord Adonis and Mr Johnson for a very lively and useful session.