

## Treasury Committee

### Oral evidence: Appointment of Richard Hughes as Chair of the Office for Budget Responsibility, HC 618

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Members present: Mel Stride (Chair); Rushanara Ali; Mr Steve Baker; Anthony Browne; Felicity Buchan; Ms Angela Eagle; Siobhain McDonagh; Alison Thewliss.

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Witness

I: Richard Hughes.



## Examination of witness

Witness: Richard Hughes.

Q1 **Chair:** Good afternoon. Welcome to the Treasury Committee and our pre-commencement hearing in respect to the appointment of Richard Hughes by the Chancellor to the position of chair of the Office for Budget Responsibility. Richard, welcome to the Committee. I wondered if you could begin, please, by very briefly introducing yourself for the public record.

**Richard Hughes:** I am Richard Hughes. I am a research associate at the Resolution Foundation and an adviser to the International Monetary Fund.

Q2 **Chair:** Richard, welcome to the Committee. We are going to run no later than 5.30 pm. We may finish a little earlier than that. Just so that the public are aware of the process we follow after that, we go into a private session, in which we will consider our report on this proposed appointment.

Let us start with coronavirus and the current economic situation. The virus has thrown many things up in the air. It has made forecasting extraordinarily difficult at the moment. Could you just run through for the Committee the particular challenges you think it has presented and how you think in forecasting terms these challenges can be best addressed?

**Richard Hughes:** You are right to say that coronavirus is an exceptional economic shock, certainly for advanced economies. We have seen pandemic viruses and epidemics hit other countries, especially emerging markets and low-income countries, in the past. For advanced economies, we have not experienced pandemics for over a century, so history is a somewhat poor guide for what to expect over the course of this kind of economic crisis.

If I were to characterise how it is different from the past shocks that the UK has faced economically and fiscally, I would highlight five things, all of which begin with S. The first is its size. Based on the OBR's latest forecast, GDP is going to fall by anywhere between 10% and 13% in 2020. The global financial crisis saw GDP fall by around 5% at its trough, so this is already twice as big as the initial impact of the 2008 financial crisis.

The second thing that characterises this crisis from previous recessions we have faced is its speed. Usually, GDP declines sharply, but not as sharply as we have seen here. As confidence gets eroded, people's confidence about their earnings outlook falls, consumers pare back and investment gets pared back. Here we have seen, somewhat artificially and forced by Government public health measures, a sharp fall in output as well as in employment. Output fell by around 25% in one month in the month of April. That is five times faster than any one month fall in output that we saw during the 2008 crisis.



A third thing that characterises the coronavirus crisis compared to past recessions is how sectorally differentiated it is. While we have seen an average fall in output of 25% in April, that has been very different across sectors. Hospitality has seen output fall by 80% to 90%, while other sectors of the economy have operated more or less normally. Businesses that can operate remotely can more or less stay in business. This sectoral differentiation of the hit caused by Covid is a challenge for forecasters, as well as for policymakers.

A fourth thing that is really quite different, which again poses a challenge for forecasters, is that we have seen a large and really unprecedented Government fiscal policy response. The stimulus that has come out of fiscal policy in the UK as well as in other countries has really been extraordinary. We have seen an unprecedented peacetime fiscal expansion so far in the order of 10% of GDP. When you compare that to the stimulus that was provided by the Government back in 2008, that was anywhere between, depending on how you measure it, 2% and 5% of GDP. It is anywhere between two and five times the kind of fiscal impulse that you have seen into the economy. Trying to judge the impact of fiscal policy on the economic outlook is itself a challenge for forecasters.

The final thing that differentiates this crisis from others is the prospect of a second wave and the re-emergence of the virus, either through regional outbreaks or through a nationwide or even global second wave, which just increases the level of uncertainty about where we are going next. Usually, you can assume, in the course of a recession or an economic crisis, that once you have turned the corner things are going to gradually get better and it is all about the pace of that recovery.

In this context, you have divergent possibilities as we go from here. One is a very upside scenario, where we quickly find some kind of vaccine or an effective treatment against the virus. On that basis, you could see a very rapid recovery of economic activity and a return of confidence. There is a prospect of a much more adverse scenario, where we see a resurgence in transmission, the need to lock down large parts of this country or other countries, and that acting as a drag on the outlook for quite some time to come.

The challenge that presents for forecasters is how we think about the fiscal outlook. We cannot just focus on the central scenario in this sort of case. We have to look at a range of possible scenarios. In that context, when the OBR comes out with its *Fiscal Sustainability Report* tomorrow, the work it is doing to look at those upside and downside scenarios is really important to making sure that, whatever the Government's policy response going forward, it is robust to that range of possible outcomes for the economy and public finances, not just based on a single scenario for the recovery of the economy and the path for public finances.

Q3 **Chair:** You mentioned divergent possibilities as to where the economy



may go from here. All of us would thoroughly agree with that. What do you read into the measures that the Chancellor chose to come forward with last week in that respect? Could it be said that backing away from furlough and going to this £1,000 bonus jobs scheme, along with the stimulus he is putting in the economy, albeit they are sector-specific, might point to him thinking that the virus is going to be more of a long-term problem, and the economy needs to adjust out of furlough and into whatever shape it is going to form afterwards? The stimulus suggests that it is not picking up as quickly, albeit it has some way to go, as we would be hoping. What do you read into the specific measures and why he went for those?

**Richard Hughes:** I would not pretend to try to get inside the mind of the Chancellor. I would say two things about the policy package. First, the classic lens through which fiscal analysts look at fiscal stimulus packages is the three Ts. Is it timely, is it targeted and is it time-limited? The Treasury has chosen measures that act quickly. They have necessarily been targeted, partly to ensure their effectiveness and partly to ensure their affordability.

They are for the moment time-limited. The JRS itself is being removed from the autumn. That is designed to create an incentive to get people back into work and back into economic activity. It is coupled with a modest incentive for employers to bring those people back into work compared to the kind of support they have had under the JRS, but most of the work is being done by the fact that the JRS itself is winding down.

There are always criticisms of these kinds of policy packages and there are inherent trade-offs between the different objectives you have for fiscal stimulus packages. A lot of the instruments that are the most effective in terms of fiscal multipliers, so the impact they have on economic activity and things like public investment, are the least timely because they take a long time to get organised and to start spending the money, so you face an inherent trade-off between how quickly and how effectively you can act.

Probably the single most important thing that the Chancellor announced in terms of stimulating activity last week was the cut to VAT in the hospitality sector, because that was a very significant reduction in taxes. It acts very quickly. VAT rates change overnight. Again, it was a time-limited incentive to encourage people to patronise a sector that so far has suffered the hardest from the economic downturn.

**Q4 Chair:** We have very low inflation at the moment, but there is a lot of stimulus going out there and we have a restricted supply side. We are not sure about where this virus is going and, indeed, whether there could be a second lockdown. What are the risks, in your opinion, of inflation spiking up at some point in the future and under what circumstances do you think that that would occur?



**Richard Hughes:** There are risks on both sides of the inflation outlook, but they are probably tilted toward the downside rather than the upside, in terms of inflation being below the 2% target rather than spiking upwards. Unlike what we saw in 2008, inflation actually fell in the immediate aftermath of the shock of the lockdown. It fell to 0.5%. In the immediate wake of 2008 crisis it actually spiked to around 5% before settling down. That is partly due to the oil price. We are importing lower inflation from the fact that energy prices are lower.

Looking forward, there are risks on both sides. The supply of money is up, but so is the demand for money. People need it for liquidity purposes, but also the velocity of money has shrunk, because the ability of money to move around the economy is much more limited. For at least a few months, people were just going to the shops and that money was going straight back into the bank. It was not going elsewhere in the economy, into the hospitality sector, restaurants or other lines of business. You needed more supply of money just to support the fact that money was doing a much shorter round trip around the economy before it ended up back in people's bank balances.

The one thing I would say, however, about inflation, particularly in the UK context, is that we have more reason to fear inflation from a fiscal point of view than other countries do. That is because around a third of our total debt stock is index-linked. It is linked to RPI inflation. There has been a lot of somewhat idle chat about the prospect of inflating our debt away in future and the fact that we do not have to worry about having elevated levels of debt, because we can just pull the same trick that Governments did in the 1950s and 1960s of using inflation to erode the real value of our debt.

That is not going to work for around a third of our debt stock, because the higher inflation is, the more expensive it gets. Both the principal and the interest payments are indexed to inflation, so we have lost one tool that we have used in the past to actually reduce our debt stock. We have reason to be more alert to the risk of higher inflation than a lot of other countries do from the point of view of concerns about fiscal sustainability.

Q5 **Felicity Buchan:** My questions are on independence from the Treasury. The raison d'être of the OBR is to be independent from Government, but you held a very senior position at the Treasury until April 2019 and have worked there for nine years in total. How can you reassure the Committee that you will be independent from Treasury?

**Richard Hughes:** It is true that I have spent about half of my career working in the Treasury, but it is also the case that I have spent about as much time working outside the Treasury as I have in the Treasury. There are real advantages in this position to having inside knowledge of the Treasury. There are a few places outside Ministries of Finance where you can get experience of macroeconomic forecasting. There are very few places outside of Ministries of Finance where you can get experience in



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fiscal forecasting. I have the advantage of both knowledge of how to do macro forecasting, and particular knowledge of fiscal forecasting.

The time I spent outside the Treasury has the advantage that I have seen how fiscal forecasting and fiscal analysis is done in other countries and how it can be done better. I came back the first time to the UK with ideas on how I could improve it.

With regard to questions around my independence or willingness to hold the Treasury to account, I would say a number of things. First, I was a passionate advocate for greater transparency, better fiscal management and greater responsiveness to Parliament and its demands, and to the public and their demands, even when I was inside the Treasury. I was a passionate advocate of having better disclosure and management of fiscal risks, disclosing more about what was going on in the Government balance sheet, improving the way we analysed and managed Government guarantees and making us more accountable to Parliament for those decisions, as well as for things like sales of public sector assets.

Even when I was in the Treasury, I was a thorn in the Treasury's side in a number of regards, but effectively so. I helped make Government more transparent fiscally while I was there. The experience of people like Graham Parker, Charlie Bean and Andy King, all of whom have been on the BRC, is that poachers sometimes make the best gamekeepers. We know how existing practices work, we know where the bodies are buried and we sometimes do the best job of unearthing them.

One final thing is that, throughout my 20-year career in macroeconomic and fiscal forecasting, I have built up a reputation as somebody who has been an advocate for objectivity and transparency in fiscal policymaking. I am not suddenly going to become, now that I am head of an institution that I was an advocate for setting up and have long wanted to be the head of, the person who brings the UK's fiscal watchdog to heel, muzzles it, turns it into the Chancellor's lapdog or whatever canine analogy you care to use. That is not what the last 20 years of my career have been about and I do not mean for it to be what the next 20 years of my career are about.

**Q6** **Felicity Buchan:** Is there a risk that you are just too embedded in the Treasury way of thinking, let us say when it comes to modelling, for instance? You have that in your blood, so to speak.

**Richard Hughes:** I have been an outspoken advocate for some pretty unorthodox ways of looking at and thinking about fiscal policy, trying to bring a greater focus on the balance sheet rather than just looking exclusively at debt, and trying to look at and manage fiscal risks rather than just focusing on a single scenario.

In those regards, I am somebody who has been an unconventional thinker, even within the Treasury. The time and experience I had outside the UK, looking at how fiscal policy is made in other countries, has helped



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to convince me that there are ways in which we can do things better in this country. I mean, were I to be confirmed by this Committee as head of the OBR, to continue that collaboration with other international fiscal institutions analogous to the OBR, to make sure that we are always refreshing the institution with those new ideas.

**Q7** **Felicity Buchan:** Do you see any areas where you were so embedded in Treasury thinking that it is almost your baby and you would be reluctant to get involved and criticise, given that you had ownership of that in the past?

**Richard Hughes:** I do not think so, except in reforms that were about making the Treasury more accountable, transparent and responsible in the management of the public finances. I guess I would see all those areas as being something that I should continue to advocate outside, as head of the OBR.

**Q8** **Felicity Buchan:** Do you have any experience of challenging Treasury?

**Richard Hughes:** I do. When I was inside the Treasury, I was the head of, for a period, the cross-Whitehall analysis that various Government Departments' chief economists did of the impact of different scenarios for the UK's exit from the EU on the UK economy and public finances. That came to a set of conclusions that were not particularly comfortable for Government. There was no scenario where the UK, in terms of GDP, was better off 15 years hence than remaining in the EU, so in that sense that was a set of objective, independent analysis that Ministers were very good at accepting, but nonetheless was not what some wanted to hear.

Outside the Treasury, working for the IMF, it was our job on a fairly regular basis to be critical of Governments' economic and fiscal policies. I did work on everything from looking at the transparency of the Russian Government's state accounts to looking at whether Greece was adhering to the structural benchmarks within the Greek support programme provided by the IMF and ECB, and holding the Greek Government to account for their performance against those benchmarks.

I guess more recently at the Resolution Foundation I have been critical of the Government's fiscal rules. I have been critical about the way the Government have managed investment projects. I have been critical about some aspects of the Government's response to coronavirus. I have not pulled my punches at any point in my career. Again, I do not mean to start once I am head of the OBR, with this Committee's blessing.

**Q9** **Ms Eagle:** Do you worry about groupthink in economics?

**Richard Hughes:** Yes, I do, although there is less of it than you might think there has been in the past. In the past, people have talked about the Washington consensus dominating economic thinking. Having spent eight years in Washington, I can tell you that I did not find that much consensus there, during the time I was there between 2008 and 2016 at the height of the global financial crisis.



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There has been an established orthodoxy around certain questions of monetary and fiscal policy, but more and more there is a much more diverse debate. When you look at the fiscal policy debate today, the idea that Governments would be spending the amounts of money they are spending to support their economies was something that no one in the economics profession would have envisaged 10 years ago. It is very much higher than we saw in the wake of the last financial crisis.

There are new theories about what central banks should be doing beyond just targeting inflation. I am not advocating any one of those here and monetary policy is eminently not an issue for the Office for Budget Responsibility, but nonetheless that debate is out there and being had after a period of consensus about inflation targeting being more or less the way of the world in monetary policy.

Like any profession, economics suffers sometimes from groupthink, but then circumstances come along that demand it to think differently. It has thought pretty differently and creatively in the wake of this particular shock, in a way that I find impressive.

**Q10 Ms Eagle:** Do you think that part of the groupthink, apart from economic fashions or even organised economic ascendancy, such as that organised by the Mont Pelerin Society in the neoliberal era, ought to be more broken up by, for example, having a more diverse selection of economists at the OBR? There are not very many women, are there?

**Richard Hughes:** There used not to be very many women at the OBR. It has come a long way very quickly, I should say. In 2017-18, it had only about 19% women, if memory serves, and today it has 41%, so the OBR has definitely recognised the need to improve its gender balance. It needs to go further to get to parity. I accept that at senior levels in the OBR it is very male and something needs to be done about that.

**Q11 Ms Eagle:** There is only one woman out of the six senior executives, isn't there?

**Richard Hughes:** Yes, that is right. Were I to be chosen as the head of the OBR, I would recognise that as an issue that needs to be addressed, in terms of putting more women in senior leadership positions in the organisation.

**Q12 Ms Eagle:** In your questionnaire, though, you were asked what you think some major challenges for the OBR were and you did not mention diversity as being one of those.

**Richard Hughes:** You are being a little unfair. I did say that making the OBR an inclusive, open and welcoming place to work for people of all genders, ethnic backgrounds and sexual orientations was one of my five priorities for the institution and it certainly would be. Were I to be before this Committee again in five years' time and looking back over my performance, I hope you would hold me to account for whether I have achieved that.



Q13 **Ms Eagle:** How do you intend to do it, then?

**Richard Hughes:** I have been in a senior management position in a number of other areas and had to do recruitment. You need to set yourself objectives for doing so. There is no substitute for going out and actively headhunting and recruiting talent. One problem that institutions have is that they sit back and wait for people to come to them. You have to do active recruitment and headhunting to achieve this.

The economics profession in general faces a challenge, which is that one-third of economics graduates coming out of university are women and the remainder are men. The economics profession still has a reputation of being a very male field. There are obligations on people like me to make it clear that that is not the case. There are already positive developments, in that you have a female chief economist of the IMF, you have a women head of the IMF, the head of the ECB is Christine Lagarde and the two heads of the Government Economic Service in the UK are both women.

The culture is changing. The image that is promoted at the top is changing, but I accept that it is my responsibility and role to make sure that organisations actually change in the way they are composed and managed.

Q14 **Ms Eagle:** Why do you think there are fewer women than men in economics?

**Richard Hughes:** It is partly the historical relationship between economics and banking and finance, which also has an underrepresentation of women. People think of economics as being a gateway degree to going into working in the City, which, in fact, is not the case. A very large number of people with economics degrees end up working in other fields, oftentimes in the public sector, in places like the Treasury and the OBR. There is more work to be done by people in senior positions to make it clear that this needs to be a profession that reflects the diversity of the society that it serves.

Q15 **Ms Eagle:** If there were more women in economics, do you think that forecasting would be done differently? For example, the current coronavirus crisis has affected women far more than men, because they tend to be in low-paid areas and they have lost their jobs. They have had to look after the kids far more at home in those families that are in lockdown. BAME people have been more affected by the disease itself and are more likely to be represented, in our unequal society, among those who are poorer and more vulnerable. Do you think that, if we had more female and BAME voices in the decision-making areas, in forecasting and in senior positions, we would get a bit more of a diverse view on policy matters?

**Richard Hughes:** It does make a difference. Bringing diverse voices into the profession and the forecasting process always brings new perspectives. It also brings different weights on economic objectives. As



you said, there is, on the one hand, the overall objective of trying to increase growth or improve per capita GDP, but there are also objectives around distribution, either of opportunity between men and women or across income levels. Bringing in different perspectives of people who have come from different parts of society or from different genders brings value to the forecasting process and breaks up groupthink.

One classic example is that we have typically seen the unit of analysis in economics as being the household, as though there was one thing that you could define as a household and it was homogenous across the economy. In fact, households are very different across the economy. There are single-parent households and dual-parent households. Households with children have very different economic experiences from households that do not have children, as anybody who is trying to work from home at the moment can attest to. Breaking up these uniform assumptions about how people behave and the pressures they are put under, especially in the context of crises, is important.

**Q16 Ms Eagle:** Domestic work has never even been counted in the national accounts, much less taken any account of. Would you like to see changes in the way we measure things, to try to be more inclusive of the efforts that people put in and give us a more holistic picture that we can then do our analytical forecasting with?

**Richard Hughes:** There is movement afoot in this sort of direction. I am sure that many on the Committee will have heard Lord Layard and Lord O'Donnell talking about the importance of thinking about economics from a wellbeing perspective, which goes beyond just looking at GDP, to looking at other indicators of wellbeing.

However, I have to emphasise that, from the point of view of the OBR's mission, we have a very clear mandate, which is to forecast the macro economy and the public finances, and to analyse fiscal sustainability. What matters for us is how the economy performs as it affects the public finances. Some of these wider measures are important to measuring wellbeing, measuring quality of life and looking at things like environmental sustainability, but in order for us to stay within our mandate, which is very important to preserve our independence and freedom of movement, we need to focus on those economic measures that actually matter to the public finances. Generally speaking, over the medium term those are the standard macroeconomic measures of growth, inflation, earnings and output.

**Ms Eagle:** What you are really saying is that economics has to change before the OBR will.

**Richard Hughes:** That is not at all what I am saying. The OBR has been one of the more innovative institutions out there. I would cite one particular example, which I would propose to carry on with. In its last *Fiscal Risks Report*, it looked at the fiscal implications of climate change and had quite a good discussion of what climate change might do to the



long-term economic outlook, but also how much it might cost to mitigate climate change in the longer term.

I would mean to take that work forward and take it very seriously in the context of the work the OBR does, but again, for the sake of living within our mandate and not colouring outside the lines, which is important for an independent institution accountable by law to you for the mandate that it is set, we need to always look through the lens of fiscal sustainability, rather than becoming a generic economic think tank with interesting ideas across a broad spectrum of issues.

- Q17 **Siobhain McDonagh:** On the difficulties of forecasting, given the impact of coronavirus, many households that we know will have built up savings, because they have not been able to spend and have not had the cost of going to work, while other households and families have had their incomes significantly reduced. How can the OBR make an accurate forecast as to what consumer spending will do next?

**Richard Hughes:** You are right that there is very differential impact of the crisis on different households. As you say, there are some households, particularly those at the upper end of the income distribution, whose savings have increased. There are other households, including some that have ended up on the JRS, that have more or less managed to maintain their incomes throughout the crisis, but are unlikely to have put very much of it away, given that they will have lost at least 20% of it from the fact that the job retention scheme did not cover their whole incomes. Then there is another group of people who will have ended up on universal credit if they were made redundant at the outset of the crisis. If you look at some real-time data on savings behaviours and on surveys, those people are actually dissaving.

This is a real challenge from the point of view of forecasting consumer behaviour and I do not plan to do a real-time forecast now, because I do not want to prejudice anything the OBR comes out with as its own forecast, either the scenarios tomorrow or the forecast that we might do in the autumn. It is a challenge because at the bottom end of the forecast people will be going into debt. What we know about going into debt during a crisis is that it becomes a drag on consumption coming out of a crisis, because people build up a debt burden, they worry about being able to service it and they rein in on consumption as a result of the debts that they have built up.

On the other hand, you have people who have built up savings, but they will be concerned about their employment and earnings outlook going forward. How quickly you can expect them to unwind those savings as the economy starts to recover by going back to shops and going back on holiday? Again, it is a difficult thing to judge, because if those people continue to be unsure about their own earnings and employment outlook, they may well continue to save at relatively high levels.



This also has an interaction with questions around longer-term interest rates and the Government's ability to borrow. The one silver lining from all this savings behaviour is that it has made it quite cheap for Government to finance itself, because there is a large pool of domestic savings looking to put its money somewhere. That has facilitated the fiscal support that Government have been able to provide the economy in the near term. How that interacts with people running down their savings over the medium term as the economy recovers is a big question from the point of view of fiscal sustainability. I am sorry if I have not answered your question, but it is a very difficult one and one that I would really have to wait until I was in situ at the OBR, with the approved risk committee, to try to answer properly.

**Q18 Siobhain McDonagh:** The Government will have guaranteed tens of billions in coronavirus commercial lending, some of which will not be repaid. How will you be able to include those loan write-offs in your forecasts in an accurate way?

**Richard Hughes:** This is a really important issue. It comes back to one of the points I raised at the outset about where we need to think differently about fiscal policy and the way we measure fiscal performance. Government loans and Government guarantees at the moment do not really show up in any of the fiscal aggregates that we traditionally look at when we think about fiscal policy, guarantees in particular because they are a contingent liability of the Government to the banking sector. They do not show up anywhere on the asset side of what the Government produce in terms of fiscal accounts because there are no assets there. We do not produce a balance sheet. The only stock that we look at in the public finances is debt.

By being outside the scope of fiscal accounts, it becomes harder to actually understand, explain and account for these sorts of things. One of the reasons why I have been an advocate for taking a balance sheet view of the public finances is because Governments are making increasingly active use of both sides of their balance sheets, both the asset side and the liability side, to support fiscal activity. We have seen that in particular stark relief in the wake of the coronavirus outbreak with Government-guaranteed loans.

The way in which, from a forecast point of view, you would account for them is to try to forecast the balance sheet. Forecast Government net worth. Look at the evolution of their assets, including the loans that they have made, as well as assets that they have guaranteed and equity investments that the Government might have made; look at how those perform relative to its liabilities; and forecast the long-term performance of Government net worth. That is the right way to do it from an accounting point of view. That is the way a corporation would do it. I do not really see why nowadays, especially as we have much better information about both sides of the Government's balance sheet, we should not be doing that from the point of view of the public sector.



On the narrow question of how we then evaluate the Government guarantee scheme, essentially we need to decide an impairment rate for these guarantees. We know that some of the firms that benefited from the loans are going to default on them. Those loans are going to be called. A certain amount of collateral is going to be put against those guarantees and a certain amount of the residual cost is going to end up on the Government's books.

If you look back at similar schemes that existed in Hong Kong in the wake of SARS, about 10% of these kinds of guaranteed loans were called. SARS was a very short, sharp shock to the economy of Hong Kong. This has already proven to be a virus of longer duration and greater severity, so you would expect more of those loans to be called than in the context of something as brief and evanescent as SARS.

As to precisely where you end up, you have to make a judgment based on what banks tell you about likely default rates and on some historical experience about likely default rates. There will be some defaulting on those guarantees and some of these loans will end up on the Government's books. Those need to be reflected in the forecast. I would do that by trying to forecast Government net worth, rather than adding it on as a footnote somewhere in the fiscal account.

**Q19 Siobhain McDonagh:** For those companies that are in a position to repay their loans, the money that they repay might have otherwise gone on corporate investment. What impact would that reduced investment have on your forecast, for example on productivity?

**Richard Hughes:** I have put on record, in writing I have done in the past on the Government's policy response, our concern that the longer the crisis goes on for, the more likely it is that Government guaranteed loans become less of a facilitator of the recovery and more of a burden on the recovery, because firms have built up large stocks of debt, which they will struggle to write off. The more that debt is a burden on companies, the less they will invest.

We know from past crises that one of the reasons why you see longer-term scarring on the economy is that you have forgone investment. That scarring can be significant. It can be in the lost percents of GDP in the long run. In terms of what you can do about it, in my past writing on this question I have advocated making repayment of these debts earnings contingent, in that firms are not asked to pay back more than a percentage of their turnover in a given year, so these debts do not become a burden on their ability to invest and at least break even, if not make some sort of profit, when they come out of the crisis.

**Q20 Siobhain McDonagh:** Would the Government be better off just not asking for some of them to be repaid?

**Richard Hughes:** In principle, that is what making them earnings contingent would be, in that it would say, "You only need to pay back 5%



of your annual turnover in any given year". By the end of the term of the loan, the sum that has not been repaid would then end up being written off and borne by the Government.

**Q21 Siobhain McDonagh:** Were you to stay on for the maximum length of two terms of five years, do you think you would oversee the OBR forecast in which the programme of quantitative easing is being withdrawn?

**Richard Hughes:** The short answer is that I do not know. All the predictions that have been made to date about the withdrawal of QE have proven to be inaccurate. That said, we have faced two of the worst economic crises this country has ever faced in over a century in the space of 10 years, so we are to some extent in exceptional circumstances from the point of view of monetary policy.

One thing I would say, which the Bank of England has said itself, is that it is wrong to think of Government holdings of debt being completely unwound by the time this crisis has run its course. That is just because overall demand for central bank reserves has gone up since 2008. That is the result of a number of factors, including changes in financial regulation, which mean that banks need to hold a lot more liquid capital. It is to do with changes in the way the monetary policy transmission mechanism works, which mean that the Bank has to rely on taking in central bank reserves and buying some kind of asset on the other side of its balance sheet, as a way of managing monetary policy and managing interest rates.

As the Bank of England itself has acknowledged, it is unlikely that the Bank of England's balance sheet will ever shrink back to what it was pre-2008. It will always have an elevated level of reserves, and an elevated level of assets in which those reserves are invested on the other side of the balance sheet, in order to perform its day-to-day monetary operations and satisfy the demand out there in the financial markets for reserves.

**Q22 Anthony Browne:** I have one question about the Treasury modelling and then some questions about the independence of the OBR. First, on the modelling, one of the frustrations with the Treasury of people who believe in lower taxes rather than higher taxes is that Treasury economists are very sceptical about dynamic modelling, by which I mean that, when thinking about the fiscal impact of tax change, they do not really consider the impact of that tax change on behaviour.

An example that is very live at the moment is that we are all about to legislate the stamp duty holiday that was announced last week. If half the tax paid in somebody moving house is stamp duty and the other half is VAT on builders and furniture, if you cut stamp duty and it doubles the number of transactions, you might expect the net impact on Treasury revenue to be zero rather than a cut. I am just wondering what you think about dynamic modelling in this way.



**Richard Hughes:** Back to Ms Eagle's question about diversity of views in the economics profession, it is an area where there remains a lively debate among economists about the right thing to do from a fiscal modelling point of view.

I would make a distinction between two different kinds of dynamic effects. There are near-term behavioural effects, which the OBR is very expert in taking into account in modelling of policies. One thing that was notable about the Government's policy announcements last week is that they did not incorporate those behavioural effects, because they had not invited the OBR to certify the costings. The OBR is going to do, as it announced this morning, its own costings of the Government policy packages that reflect those behavioural effects. That is really important to giving a complete and transparent picture of the policy package that the Government have presented.

Capturing those kinds of behavioural effects is the bread and butter of doing good fiscal modelling and good modelling of policy packages. It is not particularly controversial for anybody to say, "You should take into account the impact of stamp duty changes on the volume of housing transactions," or, "You should take account of the impact of raising tobacco duty on the amount of smuggling going on." That is absolutely an important aspect of getting the right costings of the policy.

There is a different kind of dynamic scoring that is a longer-term question, which is what the impact is of particular fiscal policy measures on the growth outlook. That is an area where there is a lot more controversy within the forecasting profession and different practices followed by different kinds of institutions.

One reason why it is particularly challenging and can be frustrating for advocates of particular policies is that a lot of those longer-term dynamic effects take effect through impact on stocks rather than on flows of income. To give you an example, it is a perennial frustration of Finance Ministers everywhere that they spend lots of money on public investment and they say, "Why is that not having an effect on our growth forecast?"

The problem is that public investment is the flow of investment into the economy. What matters for the performance of the economy is the stock of infrastructure that you have and that is the culmination of hundreds of years of investment by previous Finance Ministers. The stock of infrastructure assets in the UK is several hundred percent of GDP. The annual public investment in the UK is around 2% of GDP.

If you increase investment by 1% of GDP up to 3%, that is not going to make a very big difference to this enormous stock of infrastructure assets you have out there, which started being built by the Romans and then again got a big injection of cash by the Victorians. In the very long run when it builds up a much bigger stock, it will have an impact on things like growth. If you can forecast long enough out there, you can pick up its dynamic effects, but in the near term its marginal contribution to the



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overall value of the stock of things that matter for economic activity is relatively modest. That is one of the reasons why you tend to not pick up dynamic effects that work through the stock side of the accounts.

**Q23 Anthony Browne:** In the current example, the Chancellor just announced a range of measures to try to stimulate economic activity, in particular VAT and stamp duty cuts. Given what you have said, how would you assess the impact of those tax cuts on economic activity?

**Richard Hughes:** Collectively, they will have an impact on people's marginal propensity to consume and an effect on the timing of spending. They make it cheaper to go out there and buy a set of goods, which might encourage people to buy them rather than save the money. It also creates an incentive to buy them now versus buy them later. So long as economic activity continues in the way that we hope it does, and we head into a recovery, now is the right time to try to get consumption to recover. If you can bring forward more of that consumption now, you can hopefully support firms in the recovery of their own businesses.

In those senses, you would look at what it does to marginal incentives and the incentives it has for the timing of people's expenditure. That is taking account of classic behavioural effects on households and firms.

**Q24 Anthony Browne:** The question I had about the independence of the OBR is really about your right to publish the reports, as it were. Let us say you are required by the Act that set you up to publish two reports a year, but you can only do so when the Chancellor asks you to. Last year, the OBR was going to publish a report for the November Budget, but the Chancellor then cancelled the November Budget because a general election was called. You had this scenario where the OBR had one of its reports cancelled for what are, essentially, political reasons. Do you find that an uncomfortable position to be in?

**Richard Hughes:** Those things were a function of the electoral timetable and that disrupted a lot of people's lives and activities, some a lot more than others, including some outside the OBR. There are concerns that I have about process, however, and the way process interacts with people's ability to understand in a complete sense the state of public finances and the state of the economy. Those relate to more recent events. The last four months has been an exceptional economic shock to the UK economy. It has required the Government to move with exceptional speed and dispatch in developing a policy response.

Since March, you have seen us getting into a pattern of iterating between OBR forecasts being produced on the one hand, then the Government coming out with policy announcements on the other, and those two things being done at separate points in time. That raises three challenges from the point of view of transparency, public understanding of what is going on and fiscal management.



First, the Government policies under development are not being informed by a fully up-to-date OBR economic and fiscal forecast. There was a scenario done back in April, but the world has moved on a lot since April. Secondly, the costs of Government policy announcements are not being certified by the OBR. This picks up the point about behavioural effects and actually capturing those in doing costings, and, rather than giving upper limits, trying to build those kinds of behaviour effects into the estimations of the costs of policy packages.

The third concern it raises is that the public do not get to see what impact the Government's policy package is likely to have on the economy. There is a big question around what the impact of the job retention bonus is going to be on employment, for example. Because we do not have an employment forecast produced by the OBR, we cannot see that. That is not part of the policy debate we can have at the moment.

As I said, the situation we are in is a result of exceptional circumstances and the need for both institutions to move at speed, to try to inform the public debate. But the public finances should not be some kind of a puzzle that you, Parliament or the public have to put together by assembling different pieces, with an OBR scenario produced one month over here and a set of policies produced by the Government in another month over there. We need to find some way to bring the forecasting and policymaking processes back together, as envisaged under the Act and under the charter, which assumed that the Government were only going to be making policy announcements twice a year: once in the autumn Budget and then once maybe in a spring statement.

It is eminently necessary for Governments to make policy in real time, but we need to get back to a point where the Treasury, Parliament and the public get a complete picture of the Government's fiscal plans when they are announced, which brings together both the policy package and the forecast. We have an opportunity to do that in the autumn Budget. It really is important to get back to that as a principle of transparency in the way we explain Government policy decisions and the fiscal outlook to you as a Committee, to Parliament and to the public.

**Q25 Anthony Browne:** As you say, it has been extraordinary times, so the Government may be making policy in real time, as you call it, going ahead as well. Is one solution that you have the right to initiate your own reports?

**Richard Hughes:** The OBR has that right now and it has used it very effectively. The scenario that it produced back in April was something that it produced of its own volition. It has produced working papers looking at different aspects of the forecast. So long as it is consistent with its mandate of informing the public debate about the sustainability of the public finances, it has that right. If anything, what has prevented it from doing so is being kept so busy by fiscal events and other documents, rather than any inhibition on it in producing its own analysis.



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Q26 **Chair:** You were talking about taxes there. Are there any taxes that you have a strong suspicion, given the rates at which they are set at the moment, could be subject to some kind of Laffer effect if they were reduced? Do you think most of them would yield more if they were increased or are they already at the yield maximising rate?

**Richard Hughes:** I would be very loth to say at this stage, having not kicked the tyres of the OBR's tax models personally.

Q27 **Chair:** What hunch do you have? Where would you look if you thought you could drop taxes and get more yield in?

**Richard Hughes:** It is not my advice to give. It is not my role now and it would not be my role as head of the OBR to give the Government advice on what to do with taxes. The classic ones that you will know very well, Mel, are taxes on tobacco and alcohol. It is a constant fight against smuggling and evasion, so those sorts of taxes always have to be set with behavioural effects taken into account, although I am not in any way suggesting that, if you were to reduce the taxes on these, you would bring in more revenue. That is not the case at all, but those taxes are especially sensitive to behavioural effects.

Q28 **Mr Baker:** Richard, thank you very much indeed for coming along today. You said earlier in your evidence that you have always wanted to be the head of the OBR. Did I hear you correctly?

**Richard Hughes:** It is something that I have had my eye on for a while, yes.

Q29 **Mr Baker:** Explain why you have had your eye on it.

**Richard Hughes:** For me, it is an opportunity to carry on work that I believe passionately in, which is to provide the most transparent set of public accounts possible. It is an organisation that has a track record of innovation and has always taken on good practices in the field of macroeconomic forecasting and fiscal analysis.

As an institution, it has made a huge difference in a very short space of time. I should pay tribute to its current chair, Robert Chote, in establishing the OBR as one of the preeminent independent fiscal institutions in the world in a very short space of time. It is spoken in the same breath as the Congressional Budget Office in the US and the Central Planning Bureau in the Netherlands. The CPB was founded in the 1930s. The CBO was founded in the 1970s and took a much longer time to build up the kind of track record that Robert and his colleagues have built up in the space of a decade. For me, the opportunity to take over already such a high-performance machine in the work it does, to me, had great appeal.

Q30 **Mr Baker:** Super, thank you. This is the first time that you have been the undisputed leader of an organisation in its entirety. What will be your approach to forming your strategy as that leader?



**Richard Hughes:** I have been the leader of significant parts of other organisations, I would say, but you are right that it is the first time I would be the head of an organisation in my own right. First and foremost, you have to understand the environment in which you operate. That is especially important when the environment is changing. I have a bit of experience of coming into organisations where the environment is changing. I arrived at the IMF in 2008 when the world was changing around us very quickly. I arrived back in the Treasury in 2016, which was a time of quite great change in economic and fiscal policymaking in the UK, not least in the wake of the Brexit referendum.

Again, the OBR is operating in an environment that has changed very quickly, so getting the institution to invest in understanding how the world around it is changing and in what direction is really important to understanding where we are going next. The OBR is already doing this, but I would like to see more of it using real-time data to actually diagnose what coronavirus is doing to the economy at this very moment and where it might be going next.

Q31 **Mr Baker:** Does that put you in a similar camp to Andy Haldane at the Bank of England? I believe his main distinguishing feature in going for a V-shape recovery from coronavirus is that he has been looking at real-time data. Am I right in thinking that that puts the two of you in the same camp? Does that mean that the two of you are likely to come up with perhaps different results to consensus as we go on?

**Richard Hughes:** I agree with Andy in so far as it is important to use whatever data you can find to understand the world around you. With regard to what letter you choose to describe the economic recovery, to be honest, the letter of the alphabet that you choose, whether it is a V, a U or a W, matters a lot less than how far and how quickly you actually get out the other side.

What high-frequency data has told us so far is that there is a bit of good news, which is that we reached the nadir of economic activity a lot more quickly than we thought, in that April seems to have been the low point and activity started recovery in May. That is a lot faster than the three-month scenario for the lockdown that the OBR forecast back in April.

Real-time data has also said, as Andy acknowledged, that the trough seems to be shallower than we feared. The OBR was forecasting a drop in activity of around 35% in April. It turns out to have been only about 25%. As I said, the thing to bear in mind is that it matters less how quickly things are going down on the downslope, or how quickly they are starting to recover, than how far we are going to get back the 25% loss of output that we have already faced.

Q32 **Mr Baker:** I am so sorry to interrupt you. I am just very conscious of time and thinking that others might wish to ask you about coronavirus. I just wanted to see if you recognised this association with Andy Haldane's thinking, which you clearly are very closely in touch with.



**Richard Hughes:** In terms of methodology, yes. On the early indications of where we are getting to in the recovery, there is good news about the pace of the recovery at the high street and retail, but one of the problems we have in trying to explain the performance of the economy to the public these days is that explaining things in growth rate terms can be quite misleading. While 16% growth in retail sales sounds great, to be honest, anything less than 25% is bad news, because it means we are still on the other side of the V. The economy can be V-shaped, but until you get the 25% back we are still considerably worse off.

Q33 **Mr Baker:** Thank you very much. It has all been very helpful. To come back to you leading the organisation, you might find pressure coming up on you from the Treasury. You have had a distinguished career in the Treasury. What is your approach to standing up for the OBR against any undue pressure from the Treasury?

**Richard Hughes:** In the first instance, the approach is the same. If anyone from the Treasury were to say to me, "We would like to see this particular outcome for GDP growth or this particular outcome for the deficit", I would say, "We are going to come to our own view. We are going to publish that and we will send you the *EFO* for factual comments and corrections only". If that sort of pressure was persistent or came with an air of menace, as an attempt to impair the independence of the OBR, I would inform this Committee and the public.

Q34 **Mr Baker:** Let us hope there is no menace. That would be very sinister, but I do not think you will be subject to menace. I look forward to hearing from you if you are. Do you have any particular role models for how you should lead the organisation or any particular areas of study that you want to engage in, to develop your leadership and what is a very important role in the national life of our country?

**Richard Hughes:** My predecessor, Robert Chote, has done a really extraordinary job. I can really only hope to do as well as he has, both in establishing a really professional and effective institution, and in communicating as effectively as he does its work and its results. First and foremost, I would model myself on Robert. I can only hope to be as good a chair as he has been.

Q35 **Anthony Browne:** I have some questions about the scope of the work of the OBR, but I just want to follow up Mel Stride's follow-up to my question about the Laffer curve, without trying to lure you into advising the Government on the tax changes. When you are assessing the fiscal impact of a tax change, how do you assess whether you are actually at the peak of the Laffer curve or beyond it?

**Richard Hughes:** One thing you look at is the history of tax rates and tax takes. Have there been points where you have raised more revenue from lower levels of tax? The other is that you can have dynamic elasticities for taxes relative to tax rates, which decay over time. In this country, there are not very many taxes that are on the other side of the



Laffer curve. There probably were in the past when we had very high levels of income tax and super taxes on high levels of income, but there are not very many taxes in that category at the moment.

**Q36 Anthony Browne:** My substantive questions are about the scope of the work of the OBR. You have your two main fiscal forecasts. You assess the forecasting that the Treasury does and you cost its policies, but not the Opposition. In your written submission, you said there are risks about extending the OBR's legal mandate to include costing election manifestos of either party. What do you see those risks as being?

**Richard Hughes:** Let me preface what I might say by saying that, if this is a mandate that the Treasury and Parliament decide to give the OBR, if you want us to start to start costing Opposition policies or costing election manifestos, which is work that other independent fiscal institutions in other countries do, I would put my heart and soul into making it success.

What I would say about taking on that sort of work at the moment is that the OBR already has one of the broadest mandates of any independent fiscal institution in the world. It already has a lot on its plate in terms of understanding the economic and fiscal impact of coronavirus, understanding the Government's policy response and explaining that to the public. Giving it an additional mandate for costing opposition policies at this stage, with the resources it has, would be a significant burden on the institution and would require some quite severe reprioritisation to make space for it, in a way that might well damage our ability to do the good work we want to do on understanding coronavirus and deciphering the fiscal impact of the Government's policy response.

Other independent fiscal institutions, like the CBO and the Dutch Central Planning Bureau, do Opposition costing and cost election manifestos, but they are much better resourced than the OBR. They have hundreds of staff, rather than 38 people, to do that work. A lot of those people's time is taken up costing Opposition policies.

There is also an institutional or quasi-constitutional element to this, which is that, in the US context, legislators have much more right to initiate tax and spending policies, so it is important for the legislature to have its own costings body. The reality in the UK is that Back-Bench MPs have a much more limited ability to initiate their own tax and spending policies. You see it in the estimates debates that we have here in the UK. These things are debates essentially about one minor aspect of Government policy. MPs themselves do not amend the estimate for Departments and change the amount that they are going to spend, so I am not sure it is entirely proportionate to create a large institution that helps Back-Bench MPs to cost policies when, in fact, their ability to initiate the legislation needed to realise them is quite limited.

I worry, on the other hand, about it jeopardising the OBR's role as official forecaster for the Government. If the Government thought that the OBR



as an institution was an institution of two halves, one half serving the Government and the other half serving Parliament, and it put equal time and weight on those activities from a policy costings point, that would make it harder to maintain the confidence of policymakers in Government.

**Q37 Anthony Browne:** Presumably, it might risk the OBR's reputation for impartiality.

**Richard Hughes:** As I said, if we were given this mandate, we would look to do it with the same kind of rigour and objectivity with which the OBR has done all its other work, but it would require some pretty big governance changes to the way we manage our business, to make sure that there was no suggestion of that kind of politicisation.

**Q38 Anthony Browne:** Do you see it as the OBR's role to serve the Government, to serve Parliament or to serve the wider public?

**Richard Hughes:** The truth is that we have a dual mandate and that is actually a very good thing. We serve the Government in providing a forecast on which they base their policy decisions. We certify the costing of Government policies, but we also serve this Committee and Parliament in our obligation to explain the economic and fiscal outlook to the public and to analyse fiscal sustainability. That is a really important guarantor of the objectivity and independence of the institution, because not being either wholly dependent on Parliament or wholly dependent on Government allows us to maintain the delicate balance of being independent of both, if you see what I mean.

We rely a lot on this Committee and its support, both as a guarantor of our independence, and in giving us advice and input on our work, what you would like to see us do more or less of, as the people who speak on behalf of Parliament and who ultimately have to hold Government to account for their financial decisions.

**Q39 Anthony Browne:** We have other independent bodies, like the National Audit Office and the UK Statistics Authority, and they sometimes censure Government, saying that claims are misleading and so on. Do you think the OBR should have a role in censuring Government about some its claims?

**Richard Hughes:** I do not think it is censuring so much. Transparency speaks for itself. The OBR costs the Government's policies. It says what likely impact they are going to have on the forecast and under what assumptions. It is not the OBR's role to comment on Government policy or to censure particular aspects of Government behaviour, except insofar as it prevents the OBR from fulfilling its mandate.

From time to time, the Government have notified polices to the OBR too late for them to be reflected in the forecast. Those are areas that the OBR has had to bring to the attention of this Committee through its publications, because it has made it unable to fully fulfil its role of



providing a complete and transparent picture of the economic and fiscal outlook. In that sense, when the Government do not follow the rules, it is important to have some element of censure in the process.

I do not think the OBR should ever have a role in censuring Government policy, because it is not our role. We have lots of other commentators out there, like the IFS, NIESR and the Resolution Foundation, that are very good at criticising Government policies. I am not sure we need to add our voice to that chorus.

**Q40** **Rushanara Ali:** Good afternoon. I wanted to talk about the EU and what it means to the OBR. The UK has not requested an extension to the transition. It is still committed to securing a deal and it needs to do that by December, but many would say much sooner, because a whole series of things need to be done in preparation for the kind of deal we might have. Plenty of experts are assuming that it is not going to be frictionless and, at the other end of the spectrum, that we may not successfully secure a deal. How would you approach, as the head of the OBR, the forecasting challenges in the autumn around this particularly challenging agenda?

**Richard Hughes:** It does add another layer of challenge to producing a completely up-to-date forecast in the autumn. It certainly adds another element of uncertainty, although we will see how much certainty we have by the time we are producing a forecast in the autumn *EFO*.

I would start out by saying that the OBR's March 2020 *EFO* already incorporated what was seen to be an average free trade agreement with the EU and the economic and fiscal implications of that. A garden variety free trade agreement with the EU was already baked into the OBR's forecast that was produced back in March.

There has been an enormous disruption to the economy and public finances since then, brought about by coronavirus, and that will change the economic and fiscal outlook dramatically compared to March, but the starting point was already one in which we were assuming that the Government were successful in negotiating a free trade agreement. If we were not the case and if we were to end up leaving the EU without a free trade agreement, there would be consequences to the downside for growth and the public finances as a result.

**Q41** **Rushanara Ali:** When would you be asking your officials to start preparing for such an outcome?

**Richard Hughes:** Officials within the OBR and across Government have been preparing for a range of outcomes for years.

**Q42** **Rushanara Ali:** I understand that, but in the name of the transparency that you have been talking about, and you start from that position and so on, what would you do that allows the OBR to be prepared rather than being quite fixed? The OBR has had to stick to the stated Government objective of securing a deal, even when we are up against it and getting



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close to a scenario where even what was agreed in the past has been of concern for quite a lot of businesses and created a great deal of uncertainty.

**Richard Hughes:** A lot of the groundwork has already been done. The OBR looked at a Brexit stress test as part of its 2019 *Fiscal Risks Report*. One of the real contributions that the *Fiscal Risks Report* has made to the economic fiscal debate has been the fact that it has allowed the institution to do this kind of scenario planning and risk analysis of alternative scenarios for things like the Brexit negotiation. We have the underpinnings.

Q43 **Rushanara Ali:** Sorry, can I just interject there? Some of the public statements that negotiators have put out suggest that not enough progress is being made, given we do not have that much longer. I suppose this is my concern. Judging by what you have said so far and the preparation that has been done for years and so on, do you feel that the OBR is already fully prepared for the facts on the ground and the reality of the situation? You do not feel anything further needs to be done and there is no disjuncture between the fact that a deal has not been agreed yet, for which there are lots of obstacles, and the facts on the ground maybe being quite different to what the stated Government objective is.

**Richard Hughes:** There is always more work to be done. One of the challenges the OBR has had throughout the Brexit negotiations has been to try to get clarity about what the likely outcome of the negotiations is going to be, in particular around the detail, because the detail matters. It matters what customs revenue you are collecting. It matters what the immigration regime looks like. It matters in terms of the impact on financial services and other sectors where we collect a lot of tax. The more certainty you have about those aspects, the better you are able to forecast.

Q44 **Rushanara Ali:** In order to have certainty, when is your preference for the optimal point at which the Government secure a trade agreement, so that that can happen? What would your ideal timeline be for such an agreement, so that that happens?

**Richard Hughes:** The sooner, the better from the point of view of doing a forecast.

Q45 **Rushanara Ali:** Sorry, could you be more specific on what sooner means? Is it next month, the month after or what?

**Richard Hughes:** I presume it takes time to negotiate things. Sometimes things have to go down to the wire to get a good outcome from negotiations.

Q46 **Rushanara Ali:** That is not desirable, right? When is "the sooner, the better", in your view? What is the latest optimal, sensible point at which, in the interests of transparency and the OBR doing what it should be doing, it would be helpful for us to have an agreement, leaving aside the



concerns about business certainty or uncertainty?

**Richard Hughes:** I am afraid I cannot give you a particular date. It would depend on when the Budget would be and on the timescale leading up to the Budget. I would say, though, that the OBR has been very good at managing through all the uncertainties around the Brexit negotiations and coming up with some ways of estimating the impact of a potential outcome for the economy and public finance.

Q47 **Rushanara Ali:** Turning to the Government's intention to secure free trade deals with lots of other countries, at what point would you include those in an OBR forecast?

**Richard Hughes:** At the point they were secured, at the point that they were announced and agreed on both sides, it would be the right point to reflect them in the forecast, the same way that when Government have a firmly announced policy in any other area it would be the right time.

Q48 **Rushanara Ali:** At what point would your preference be that they are secured?

**Richard Hughes:** Again, I recognise that negotiations are negotiations. They are relatively small part of what we do in terms of forecasting, so it is not for us to define the timescale.

Q49 **Rushanara Ali:** I have a question about the terms of reference. In response to an earlier question, you talked about some of the benefits of considering the impact, for instance, of climate change. You also mentioned wellbeing and other indicators, but climate change you singled out as an area that is beneficial for us to think about through the work of the OBR, if I understood it correctly.

Is there a sense from your observation and engagement with the OBR, as you, hopefully, take over, that the terms of reference and the stated objectives of the OBR are fit for purpose and appropriate, having been through the financial crisis, the OBR coming into effect and now the coronavirus crisis and Brexit? Are there areas where you could envisage a role for us to look at a slightly broadened agenda or would that be risky? Would that lead to scope creep or would it be sensible for us to look at those areas, in light of coronavirus and the big shocks that this country has faced or the world economy has faced?

**Richard Hughes:** The OBR has a very clear mandate, which is really important to maintaining its independence. It focuses on analysing the sustainability of the public finances. It has broad scope and discretion about how to interpret that. It also takes account of a variety of views from stakeholders, with this Committee being one of the most important stakeholders in terms of how it actually achieves that work.

Why climate change is important to that mandate of fiscal sustainability is that it relates to the long-run sustainability of the economy. It has implications for the Government's ability to collect tax in the future from



fuel duty and other energy-intensive aspects of the economy. It also can carry huge costs in terms of climate change mitigation.

**Q50 Rushanara Ali:** Sorry, Mr Hughes, I just wanted to pick up on this. This pandemic has exposed the fact that sustainability and resilience around health in our population and the world population is critical to economic wellbeing. Do you feel that the current mandate of the OBR takes that into account sufficiently? Should we be reviewing that and learning what else could be done? It is probably one for when you have your feet under the table but, given that climate change on the one hand and now health are bringing it into sharp focus, is there more that we should be doing and thinking about?

**Richard Hughes:** Tomorrow you will see the OBR produce its next *Fiscal Sustainability Report*, which is done once every two years. It covers these issues of environmental sustainability. The health outlook is a vitally important component of the long-term fiscal picture because it determines the long-term cost of the NHS.

I would note that this Committee has very rarely had a session on either the *Fiscal Sustainability Report* or the *Fiscal Risks Report*, but they address these very questions that you are asking. I would really encourage the Committee to take up, under my tenure, these kinds of reports, because they are outside the usual cycle of *EFOs* and Budgets, but they address a much more fundamental set of questions around the risks to and long-term prospects for the public finances. They provide the basis for an informed debate, on which you can also draw analysis and information from other groups, like the European Commission and other groups that can speak more freely on policy questions, which the OBR cannot because of the mandate we have.

I would personally be loath to turn the OBR into an institution that could just become a talking head on fiscal policy issues, because it is those sorts of things that get fiscal councils into trouble and side-lined by Governments, because they do not want another set of policy advisers. They want some forecasters and people who provide a clear account of what is going on in the public finances to the Government.

**Q51 Rushanara Ali:** I have a supplementary to Angela's question about diversity. I welcome the figures you gave on gender in the OBR. Especially in the context of the Black Lives Matter protests, some would argue that institutions have got better at reflecting some areas of diversity, such as gender, although not in senior management, but not other areas of diversity, particularly race, but also a whole series of other groups with protected characteristics. Could you say a bit more about your plans to promote genuine diversity across the organisation, across different protected characteristics, particularly in the light of the recent debates around race equality?

**Richard Hughes:** This is vitally important. It is important that any institution reflects the diversity and richness of the society it serves. The



OBR, as with the gender balance, has made quite a lot of progress in diversity on ethnicity in the recent past. In 2017-18, only about 11% of staff from the OBR, based on surveys, were from ethnic minority backgrounds. Last year, it was 23%. It is really important to maintain and build on that diversity of staff. The same is true of sexual orientation and socioeconomic background.

This is important to forecasters in particular, because it comes back to this issue of groupthink and just focusing on the particular concerns of one part of society. We all bring to our day-to-day interactions and our work these inherent biases about what matters to society as a whole, but if we do not represent society as a whole we are not actually reflecting it.

**Q52** **Rushanara Ali:** There are lots of complaints about the fact that regions are often left out, just picking up on issues about social class and regional inequality. It has taken a long time for Government and institutions to take seriously regional inequality and social class inequalities. There are lots of criticisms about the elites, whatever that may mean. Most people who happen to belong to the elites do not think they do.

The fact is that many people feel left out. Right now, as Angela and others have mentioned, there has been a massive problem of disproportionate impacts on certain groups because of Covid. The danger is that the Treasury and those who analyse what Government policy is, like the OBR, are not going to learn quickly enough in terms of the analysis on what it means for different populations. Therefore, there will be question marks about your attempt to be more transparent and accountable to the public.

How do you intend to respond to the differential impacts? How does that feed in, in terms of analysis and making sure that those dimensions to Government policy are properly analysed, so that the public can actually scrutinise it? There is a great deal of frustration building up across our society, which was already there over the last 10 years. Because of the high death rate in certain communities, that is at boiling point. Institutions are going to rightly get it in the neck if they do not rise to the challenge. That will include the OBR and it will be understandable.

**Richard Hughes:** These are important challenges for all institutions and I completely recognise that, in the way they do hiring, in the way they present themselves to the outside world and in the way they think. From my point of view, making sure the OBR is a diverse organisation across the dimensions of gender, ethnicity, sexual orientation and socioeconomic background is important. I will encourage the Committee to hold me to account on the progress that we manage to make in that area.

On the question of analysis, this comes back, however, to mandate. The OBR's mandate is to forecast the macro economy and understand its implications for the public finances and long-term fiscal sustainability. There are lots of other organisations out there whose mandate relates to distributional issues. Again, it comes back to a question of mandate



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creep. It is not our role to criticise the distributional impact of Government policy and, once we do, there starts to be an element of value judgment to what we are doing, rather than just doing a forecast and analysing sustainability.

The Treasury produces distributional analysis. It put some out last week looking at the impact of the policy package that the Government announced. I know this Committee has talked to them on a number of occasions about how that can be improved. That obligation lies on the institutions that make policy rather than the institutions that do the forecasting, because they are the ones that can do something about it.

Q53 **Chair:** That brings us to the conclusion of this session. Richard, thank you very much for appearing before us. Before we go, I have one final question to you. Before we go into our deliberations in private in a moment, is there any final thought that you would like to leave with the Committee?

**Richard Hughes:** I really recognise the important role this Committee plays in the work of the OBR, both as a principal customer for our work, and, as I said, as a guardian of its independence and its mandate. If you judge me to be a worthy successor to Robert Chote as chair, I really look forward to working with you in the coming years, to continue that equal partnership.

**Chair:** Thank you very much for that and for your time this afternoon. It has been interesting to learn a little more, not just about you and your thoughts on the role of leading the OBR, but about the economic issues we have discussed, so thank you very much indeed for that. That brings us to the end of this session. We are now going to go into private session to consider our formal report.