George Osborne: Stability before tax cuts

In a speech about economic policy in the New Global Economy, at the Cass Business School in London, Shadow Chancellor of the Exchequer, George Osborne, said:

"We will share the proceeds of growth between public services and lower taxes. Over an economic cycle output will grow faster than public spending. That is the sustainable path to lower taxes. It will make Britain more competitive and protect public services.

But stability will always come before promises of tax cuts. If the public finances are in a mess then sorting them out will have to take priority over promises of tax cuts.

That is because stability, fiscal responsibility and competitiveness all come together in the new Conservative approach to the economy.

Stability to protect your mortgage;

Responsibility to look after your family budget;

Competitiveness to provide jobs and prosperity in the years to come."

Notes to Editors:

Full text of the speech below:
(Check against delivery)

"Students from more than 80 nations come together here at the Cass Business School to participate and prosper in the new global economy that is enriching our lives, shrinking our world and transforming the way we think about business and economics.

That change has already had a profound and beneficial impact on Britain. We may have just lost our place as the world's fourth largest economy to China, but it is the Chinese worker who has helped bring us the low inflation and low interest rates which we have all enjoyed since the early 1990s. In the last decade alone the price of our imports has fallen by a third relative to our exports and brought us a windfall economic gain.

It is as nothing compared to the change that is coming. In the next decade two billion people living in what were once among the poorest countries on the planet will become participants in that global economy. Not just in China, or in India, but in countries like Vietnam, Brazil, South Africa and Indonesia. All producing goods that we will consume. And in turn, we hope, consuming goods that we produce. For by 2015 annual consumer spending in these emerging economies will have doubled to more than $9 trillion, almost the level of western Europe today.

We should not fear the new global economy; it is bringing unprecedented opportunity and prosperity; it is liberating and exciting; but we must face up to the new challenges it brings.

There is the challenge of competitiveness: how we attract new investment as travel and technology make it easier for companies to locate anywhere in the world.

We should be asking ourselves some hard questions about why Google, Microsoft, Oracle, Apple and Intel have all chosen to base their European operations in Ireland and not in the United Kingdom.

And then there is the challenge of how we move up the value chain. For skills are becoming the new battleground of the global economy.

In recent years we have had to come to terms with the loss of low value, low skill jobs to Guangdong and Bangalore. Over a million manufacturing jobs have been lost in Britain over the last eight years. Now it is the high value, high skill manufacturing and service jobs that we will have to fight for. JP Morgan's recent announcement that it is moving 30 per cent of it back office services to Mumbai is the shape of things to come.

When I visited a semiconductor factory in Shanghai last autumn I asked the Taiwanese-born, American-educated finance director why they had located in China when labour costs were not an important part of their business. "It's simple", he said. "Where else can you find such a large pool of skilled engineers?"

India, perhaps. Between them, Chinese and Indian universities are turning out 4 million graduates a year – highly skilled, flexible, hungry for a chance to work hard and better themselves. That should set alarm bells ringing here in Britain where the OECD's most recent report on our economy identified a lack of skills as one of our greatest weaknesses.

And there is the challenge of how we engage businesses more in meeting the new social and environmental consequences that come in the wake of the global economy – the fact that some communities here in our own country are being left behind; that one whole continent, Africa, is left behind; and that rapid economic growth brings with it the threat of pollution and climate change.

When David Cameron first talked about companies being aware of their social responsibilities, some suggested that he was attacking business – even though in a world of global brands, where consumers increasingly care about the values of the firms they buy from, being socially responsible makes good business sense.

I suggest they read the words of the managing director of McKinsey in the Financial Times earlier this month when he identified this as one of the most important issues facing the business world in the next decade. "Business leaders", he said, "must demonstrate more forcibly the case for business in society and the massive contribution it makes to social welfare” (FT, 13th January 2006).

All these challenges of the new global economy require new, innovative and long-term thinking from the British government if we are to meet them.

But instead, sadly, we see a government increasingly paralysed by its own internal battles, afraid of reform, unable to provide the leadership that is required.

For let us look at what Gordon Brown’s response has been to the new global economy.

He has increased taxes at a time when our competitors are reducing theirs.

He has dramatically increased spending as a share of national income at a time when our competitors are controlling their spending.

He’s borrowed in a boom, run a deficit when he projected a surplus and manipulated his own golden rule when he was about to breach it.

He has added to the burden of regulation on business to the tune of £40 billion, driving business investment to a record low, when other countries are deregulating and lifting the burdens on their businesses.

He set productivity growth as his “fundamental yardstick of economic performance” and has seen it fall to a fifth of the level he inherited.

He has frustrated each significant attempt to reform the public services and improve their productivity. He is the roadblock to reform.

He has added more than 600,000 people to the state payroll while presiding over falling private sector employment in parts of the country like the Midlands.

The Chancellor enjoys lecturing other European nations on their economic performance. But our tax and spending levels are soon set to be higher than Germany's, our productivity growth lags well behind France, and our rate of business development is shrinking at a time when it is rising across the rest of Europe.

There could hardly be a worse response to the challenges of the new global economy.

And the tragedy is surely this: Gordon Brown could have done so much in what Mervyn King recently called "the nice decade". With low inflation and low interest rates around the world, harnessing the supply side reforms of the 1980s and fiscal discipline of the 1990s, he had every opportunity to build Britain into the most open, dynamic, innovative economies in the world.

He started well by giving the Bank independence and sticking to prudent Tory spending plans. But then he lost control of spending, raised taxes by stealth to pay for the spree, let borrowing soar, regulated too much, and stopped the public service reforms that might have improved productivity and given taxpayers value for money.

That is why Britain is falling down the league tables of the world on growth, on competitiveness and on trade.

The story of the Brown Chancellorship is now writing itself: a golden legacy inherited and a golden opportunity missed.

It is time to offer the country an alternative approach that rises to the opportunities and challenges of the new global economy.

In my very first speech as Shadow Chancellor, here in the City, I set as the central ambition of Conservative economic policy this: that in an age of fierce global competition, faced with intense pressure from lower wage lower cost economies, we achieve a sustained, long-term improvement in living standards.

How do we do that?

First, all our economic policies must reinforce the macroeconomic stability which we have enjoyed for fourteen years.

In part that stability has been brought about by a global phenomenon of low inflation and low interest rates; and in part it has been due to successive improvements to the macroeconomic regime: from the introduction of inflation targeting in 1992, the publication of the independent *Inflation Report* and the minutes of monetary policy meetings, and then the granting of independence to the Bank of England.

David and I are totally commitment to that independence. In the future we will also be exploring ways of entrenching it still further. The independent Bank is one element of the triple-lock on stability which David committed us to out in his first major speech as Party Leader.

The second element is an independent office of national statistics, so that we have a true account of the nation's balance sheet. Failing to include PFI and Network Rail liabilities is a clear affront to the transparency of government and the credibility of the sustainable investment rule.

I am delighted that Gordon Brown has now followed our lead and we will watch closely to ensure that he does indeed create statistics that are truly independent of government. I have sent him a draft Bill to help him do that.

We have yet to persuade him to adopt the third part of our triple lock: independent assessment of both fiscal rules. This is curious as he supported the idea when he was Shadow Chancellor. Without this independent assessment the fiscal rules are meaningless. For, as the manipulations of the last year have shown, the golden rule has no credibility so long as the Chancellor is the judge of his own performance against the rule and can alter the start and end dates of the economic cycle on a whim.

The triple-lock reinforces stability because it promotes fiscal responsibility.

That responsibility is badly needed today. Ever since Gordon Brown departed from Tory spending plans he has predicted that the books would balance in three years time and they never have. He predicted that he would have to borrow £11 billion over the past five years, or £450 for every family. Instead he has had to borrow £111 billion, or £4,450 for every family. He had to increase borrowing again in December as the deficit deteriorated.

The underlying cause, of course, has been the huge rise in public spending. The share of national income taken by the state has, according to the OECD, risen from 37.5% just five years ago to 45% today.

The new economics of globalisation mean that such fiscal irresponsibility does not, as it might have done in the past, cause an immediate run on sterling and a phone call to the IMF. That is because there is a greater supply of credit from savers across the world.

It does, however, put stability at greater risk in the long term. These days government can borrow more for longer; but the bigger the debt and the bigger the imbalances, so the bigger the potential shock and the bigger the risk to stability in the future. Global capital flows mean that the credit can rapidly go elsewhere. What happens when the savers of Asia start to spend?

All of this is why, as both David and I have said, we need a new approach that puts fiscal responsibility at the heart of tax and spending decisions. It is called sharing the proceeds of growth.

As the economy grows, we will share the proceeds of that growth between spending on public services and reducing taxes. Over an economic cycle output will grow faster than public spending. We aim to use the surplus growth to lower taxes.

But let me make this crystal clear today: we will put stability before tax cuts. If the public finances are in a mess then sorting them out will have to take priority over promises of tax cuts.

Our approach of sharing the proceeds means, first, that stability is paramount.

Second, that government is encouraged to look at ways of reducing long term demands on the state. The public sector is prevented from taking an ever-increasing share of our national income.

And third, over time, the government is able to lower taxes in a way that is sustainable and for the long term. This is crucial for Britain's ability to compete in the new global economy.

Our approach of sharing the proceeds is very different from what Gordon Brown does. He uses the entire proceeds of economic growth (and more) to pay for his uncontrolled spending. He has created a tax ratchet. In every Budget, the ratchet turns as taxes are forced to rise and tax complexity increases. The increase in oil taxes is the latest example. It is making Britain less competitive, hitting family tax bills and jeopardising jobs.

So promoting that competitiveness must be the other key goal of Conservative economic policy. For stability without competitiveness is akin to sclerosis.

Sadly, the evidence is that Britain is struggling to compete. We have fallen in the world competitiveness league from 4^{th} to 13^{th} place. Our productivity growth – that fundamental yardstick of economic performance – has slumped and the gap with the United States has widened.

Making the British economy more competitive requires a new supply side revolution. We understand that an economic policy is much more than a tax policy.

We need to improve the skills of our workforce which have been identified as such a weakness.

We need to overhaul our creaking transport infrastructure.

We need to tackle the over-regulation that imposes such a burden on businesses large and small.

We need to examine our planning laws and our competition regime.

We need reform so that poor public sector productivity no longer acts as a drag anchor on the productivity of the whole economy.

In short, we need a new supply side revolution that equips Britain for the new global economy.

I can announce today that Simon Wolfson, Chief Executive of one of Britain's most successful retailers Next, has agreed to co-chair with John Redwood our Policy Group on Economic Competitiveness.

Over the next eighteen months that group will undertake the long-term thinking required to reverse the decline in Britain's competitiveness and come forward with the policies needed for the new supply side revolution.

It will work alongside the independent Commission on Tax Reform which I have already established. The Commission is looking at the growing complexity of our tax law, how our tax system compares with our international competitors, and how we can move as a country towards a simpler, fairer, flatter tax system more appropriate to the twenty first century.

For tax is crucial to the competitiveness of the British economy too. In 2000, 20 out of the 30 major countries of the OECD had a higher corporation tax rate than Britain. Today, five years later, 20 have a lower tax rate.

If you think that does not matter then consider this: companies locating in Britain have to achieve a 25% increase in profits to achieve the same distributable income as the same company in Ireland, because of that country's tax regime.

Tax matters, but it is one part of a broader agenda of helping Britain compete.

So let me summarise.

We will share the proceeds of growth between public services and lower taxes. Over an economic cycle output will grow faster than public spending. That is the sustainable path to lower taxes. It will make Britain more competitive and protect public services. But stability will always come before promises of tax cuts.

That is because stability, fiscal responsibility and competitiveness all come together in the new Conservative approach to the economy.

Stability to protect your mortgage;

Responsibility to look after your family budget;

Competitiveness to provide jobs and prosperity in the years to come.

In other words, the right approach to the new global economy."