British Government@LSE lecture

The road to recovery – What can Government do in the current economic crisis?

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Good morning. Today I'm going to talk about the economy. I'm certainly in the right place. For more than a century LSE scholars have been at the forefront of every major economic debate asking - and answering - the most pressing questions of the day.

Today, the big question facing governments is this: Given the unprecedented pressures in the global economy, what can we do to restore stability and encourage growth?

The Coalition will be saying more about that between now and our Autumn Statement, but I wanted to make this speech today because the international situation has changed dramatically. It is worse, even, to just six months ago. To quote Christine Lagarde, the new head of the IMF: 'We are in a dangerous new phase'. A huge rise in oil and food prices. A slowdown in overseas markets. Continued turmoil in the Eurozone. Ongoing uncertainty in the US. Far from a one off shock, the 2008 banking crisis has set off a chain reaction that continues to reverberate around the globe.

And here in the UK, we are still feeling the pressure. This week we've heard that inflation is still high at 4.5%. And, in the last hour, we've been told unemployment has risen.

So, the reality we face is stark; there is now little margin for error. But that does not mean we are helpless. It does not mean we intend to sit on our hands while the global economy falters.

Our critics say that all this government is capable of is cuts. That, beyond lowering a few business taxes, reducing a bit of red tape there is little else we are willing or able to do. That is absolutely wrong. We can do more, we are doing more, we will do more. Internationally, promoting cooperation, discouraging our global partners from turning inwards. And here in the UK, where, yes, we must stay firm on tackling our deficit but, at the same time, where there are levers we can pull to stimulate growth, not least to deliver infrastructure - something I want to give special attention to today.

First, international cooperation. As important today as it was in the weeks that followed Lehman Brothers' collapse, but even harder to achieve because, for so many of us, the options available now are even fewer than we had then. And, everywhere, governments are calculating the trade off between protecting their national interests and working together for our collective good. That is a false choice. Our fates are tied.

We urgently need to rebalance global demand and unwind dangerous imbalances. Having contracted for a while, the imbalance between countries in deficit and in surplus has widened again. Countries with large deficits and fiscal vulnerabilities must put in place credible fiscal consolidation plans, pushing forward structural reforms to improve their competitiveness, and surplus countries must actively increase domestic demand, keeping their markets open. Beggar-thy-neighbour approaches may be attractive now. They will be less so if, in another three years, we're still not out of this mess.

In terms of the Eurozone, the real failure has not been the original concept of monetary union. It's that the rules were never applied stringently enough. The Stability and Growth Pact was actively watered down in 2005, allowing members to wriggle out of their fiscal commitments to each other. Now we are seeing the effects.

But on a day like today, when people are talking openly about the possibility of Greek default, the key question is not: how do we seek to renegotiate the UK's place in the European Union in a treaty that hasn't even materialised yet. The single-most important question, the urgent question is what role can we play in helping the Eurozone avoid further turmoil, creating the stability needed for prosperity and jobs – in the Eurozone and in the UK too. A stable, healthy Eurozone matters massively to the UK. It's where we send 40% of all of our exports and, together, we all face a longer term problem of competitiveness - a problem not even a raft of new treaties could fix.

So beyond the immediate issues surrounding fiscal and monetary policy, what we need is deepening and widening of the Single Market. The world's largest, borderless marketplace – designed by a British Commissioner. A market that already adds £520bn to our shared economy and, if liberalised, in services and digital industry, could add £690bn. As Europe undergoes a period of longer-term change, that should be the UK's real priority – completing the Single Market is how we put UK's interests first.

We also need international cooperation to bring stability to our international banking system. Working together to implement agreements on bank capital under Basel 3, agreeing a common approach to the extra capital the most systemically important banks should hold. And, we need to get our act together on trade. Many countries are – so far at least – resisting the lure of protectionism, but progress on trade liberalisation has dramatically stalled. It would be a huge mistake to give in to that deadlock, to give up on the Doha round worth £110bn to the world economy every year. History shows that protectionism invariably follows in the wake of global economic slowdown. Our task is not to repeat history, but to learn from it. Yes, we do need to be realistic – progress will be slow. And Doha doesn't cover everything, for example on services and investment. So we must keep pushing on bilateral agreements, between the EU and others. Working harder to bring the EU and the US together – the world's largest economic areas.

So that's what we are striving for internationally. What about here, in the UK? The Coalition has always said our first priority is tackling our deficit. When we came into power our deficit was bigger that Spain's, Italy's, Portugal's, even Greece's. Because we set out a decisive plan to reduce it, we have not been picked off by the markets. As the OECD repeated last week, our plan remains right for the UK.

So there will be no deviation on deficit reduction. We knew our recovery would be choppy. We knew our political opponents would holler endlessly for a Plan B, even though their path leads to soaring interest rates and crashing credibility. That is the luxury of opposition. But, to those who say: "the facts have changed" - yes, they have. The economic context is much worse than before. But – more than ever – we have a responsibility to hold our nerve, seeing through the difficult decisions; maintaining market confidence; creating a platform for growth.

But let's get something straight: this is about economics. Not ideology. Not stubbornness. And our plan doesn't put a straitjacket on policy. Credible fiscal policy allows us to retain loose, responsive monetary policy. And our plan allows for the automatic stabilisers to work.

So the Government is not blind to the deterioration of the environment in which we operate. More needs to be done for our recovery – that's obvious. But deficit reduction was only ever intended as a means to an end. It's a fiscal framework to ensure stability and there are other, crucial steps we must take to deliver growth.

So what can government do for growth? Let's start with the wrong approach. It's a mistake for government to try and do everything. Before the crash, the previous Government's economic record, flattered by years of unsustainable household and government borrowing, led them to believe government was the only thing that mattered for the economy. Gordon Brown, as Chancellor and then Prime Minister, believed the money would never stop flowing, that whole communities could be sustained by public sector spending, that private sector growth could be driven by endless initiatives from the centre.

But the money did stop. And, despite over 3,000 schemes aimed at business support, an array of incomprehensible tax break, endless so called 'business solutions', business investment simply did not grow in the way it should have.

Whitehall cannot grow an economy. We need the ceaseless experimentation of thousands of businesses, private saving and investment to channel money where it is most productive. Equally, government shouldn't do nothing. Deal with the deficit, but then step back in the hope a thousand flowers will bloom.

That's as bad as trying to do everything, wishful thinking at its worst.

Take regulation. Some people will tell you: all regulation is bad for growth, the hallmark of the meddling state inhibiting the functioning of a market economy. That simply isn't true. Some rules are a problem: usually endless form-filling and unnecessary red tape. That's why we're looking across the board to reduce that burden. But some regulations are positively pro-growth. Instances of the state stepping in to protect businesses and support industry, like patenting rules – encouraging our creators to invest in new ideas - or competition law – ensuring the best can expand, the worst leave the market, and new players enter too.

Rather than do nothing, rather than do everything governments should do less, but do it better creating the conditions for growth. Like in tax, where this Government is simplifying the system and reducing corporation tax to make us more competitive. In our banks, where we have this week welcomed proposals to ringfence retail banks, protecting them from the volatility of global investment banking. That reform will take some time and in the short term our priority must remain, first and foremost, to get the banks to honour their commitment to lend £190m to businesses this year. In skills, where we're maintaining cash investment in schools, creating hundreds of thousands of new apprenticeships and taking what are controversial decisions on higher education funding to keep our universities world class. All supply side interventions to make the UK a better place to invest and do business.

But this isn't just about supply side reform. You have to think about demand too. Our troubles have very much been a demand crisis. The banks' sudden withdrawal of funds, asset price falls, volatility in the markets – all hit demand. And even if we had the least regulated, most skilled, most competitive economy on the planet, if no-one spends any money, that's not enough. Clearly, with debt so high – private and public – we have to be realistic about the restraints on boosting demand. And I've asked Vince Cable to do some work on how we create the environment and incentives for business to free up new capital now. When we need them to, rather than hold off.

And that brings me to infrastructure, because investment in infrastructure stimulates demand not overnight, but more quickly than many supply side measures. And it raises productivity well into the future too. Not just any infrastructure – we need to be clear about that. The previous Government took a kitchen sink approach: any and all capital spending constituted pro-growth investment. But that's not true. Most capital spending is worthwhile. But it doesn't all support long-term prosperity. You have to be ruthless, focusing on the investments that transform growth potential: transport, energy, digital communications. Roads and rail so manufacturers can transfer goods. Better broadband so small, high-tech companies can flourish. Renewable energy so low-carbon industry can too.

If you modernise this kind of infrastructure you stimulate activity in the shorter term and you build systems high growth industries can use for years to come. Transport schemes announced in the Spending Review, for example, will deliver major boosts to growth. Like the Switch Island link road in Merseyside, where £20m of Government investment will generate 35 times that in economic benefits. Or increasing the capacity of the M62, which will generate over £1bn for GDP. Investments that will keep on giving. The kinds of investments the UK needs.

We may be one of the best countries to set up and run a business. But we rank 28th in the world for infrastructure. A nation that once led the way in engineering and construction. The home of Wren, Brunel, Stephenson. It was Tim Berners-Lee, a British scientist, who developed the World Wide Web. Yet we rely on water and waste networks from the 19th Century. Our railways are a throwback to the 1970s. We have some of the most congested roads in Europe. While our competitors continue to invest in cutting edge infrastructure.

The approach has been too incremental. Haphazard. Slow. Governments have focused on specific projects instead rather than setting out a vision. Costs stayed high and investors took their money elsewhere. That has to change. So, last year the Coalition produced the UK's first ever National Infrastructure Plan to deliver the world-beating infrastructure our businesses need from High Speed Rail, to Cross Rail, to green energy, to the best superfast broadband network in Europe. And we're galvanising around that plan with renewed energy. A gear shift in government to unblock the system and get the money out the door.

First, money. Infrastructure doesn't come cheap. So, over the spending review period, we have matched the plans of the previous Government for capital spending at least, in each year. We're protecting spending in science and research, investing, for example, in new technology and innovation centres around the country. If we had more money, we would spend more on infrastructure, but there's no longer a tap in Whitehall, to be turned on in times of need and the absolute crux of this is stimulating private investment too.

One way is by leveraging private money through public funds, as our Regional Growth Fund does. For every £1 of government investment, the private sector is putting in £5 to create thousands of new jobs targeted at areas too dependent on the public sector. I've asked Michael Heseltine and his panel, when reviewing bids for the second round, to prioritise infrastructure projects that will deliver sustainable economic growth. And I'll be chairing a meeting of Ministers to begin looking at them this afternoon.

Our Green Investment Bank will also leverage funds for low carbon infrastructure, in the region of an extra £18bn by 2014-15. Vince Cable is ensuring Government identifies the first projects to get support faster than originally planned, looking at those from next month to get them moving as quickly as possible. And Chris Huhne will shortly be setting out our support for renewable energy – a year ahead of schedule - providing certainty for investors, capitalising on the UK's position as the largest market for offshore wind.

We're also ramping up our sales pitch. We know that the UK misses out because investors simply don't know the opportunities on offer. We know they hesitate if they don't see a long-term strategy. So I've asked Lord Green to use his Trade and Investment Committee to get our plan out there. Next week, Lord Sassoon will travel to Canada to pitch to pension fund investors. Later this month, Lord Green will do the same to leaders of the Gulf Sovereign Wealth Funds. We're targeting the Middle East, Latin America and China, where there are investors with five year investment plans of over £150bn each. We're also going to be much more proactive with institutional investors here at home too.

Finally, finding the money isn't just up to us. The Cities Minister, Greg Clark, and I met with representatives from our big cities last week. They are desperate to deliver the infrastructure their cities need. So we're drawing up new money-raising powers for councils to do that where they can borrow against future growth from locally raised business rates. Tomorrow Philip Hammond will also set out our plans to giving communities more power over the funding and decisions for local transport schemes.

So: as much public money as we can afford; a hunt for private investment; new money-raising powers for local communities. But we also have to make sure that money gets spent. There are a range of obstacles that can delay new infrastructure. Planning is most often cited. That's going to change. Under our plans, if a development is sustainable, the starting point is: it will go through.

Socially sustainable, economically sustainable, and environmentally sustainable. Those reforms are the subject of some debate, but let me lay a few myths to rest. This isn't anything-goes-planning, or the death of the countryside. We are putting local people in the driving seat in a way they never have been before. Scrapping top down, regional decision-making so local people can choose the areas they want developed – and those they don't. And, crucially, making sure they get the roads, rail, housing and other infrastructure their community needs.

The other barrier I want to talk about is actually within Government: Whitehall. Identifying projects and funnelling cash to them can take time – I understand that. These are big investments, and you have to get them right. But failure to deliver major infrastructure projects on time, on budget, is a perennial problem in the UK. The extension of the Jubilee line – delayed by over a year, costing an extra £1.4bn. Wembley Stadium – meant to open in 2003; didn't open until 2007. Improvements to the West Coast Mainline – should have cost £2bn and been completed in 2005 - didn't finish until 2008, and cost four times that much. The list goes on and on. And too often, Whitehall is part of the problem. We have to break this cycle. The country needs jobs, and time is no longer on our side.

So Whitehall will put its foot on the accelerator, making sure we deliver on our commitments. To that end, I can announce that we're going through the nation's capital spending plans to hand-pick up to 40 of the biggest infrastructure projects, the ones most important to growth, which will be given new special priority status.

Each will be rigorously examined by Ministers to make sure there are no delays, no blockages and the economy feels the benefits as quickly as possible. That includes, for example, high speed broadband rollout, work to transform the efficiency of the national grid, major improvements to the rail network, like Crossrail and Great Western Electrification and projects to reduce congestion on our road network. Targeting pinch points on the M1, the M25, and elsewhere.

Where we need to get investors and developers in, we'll do so. Where local conversations need to happen, we'll make them happen. Whatever the problem is – regulation, funding, procurement, planning - if we can help unblock it, we will.

Good work is already happening. For example, by Philip Hammond and his Transport team, responsible for a huge chunk of Government infrastructure investment. To make sure it happens across the board, Danny Alexander, the Chief Secretary, will be tasked with shaking the Whitehall tree so no-one is stockpiling capital that can be put to good use today. Danny has, this week, left Cabinet Ministers and top civil servants in no doubt of their responsibilities. Secretaries of State will have to report back to him on their progress throughout the Autumn - and no one likes falling out with the Treasury.

Since we came into government Ministers have been expected to make savings. Now they're under the same pressure to spend the money they've got and, on top of all that, we'll also soon be announcing our plans to boost to housebuilding -still its lowest since the 1920s.

So, to finish as I began, Government is not helpless. The Coalition is not reluctant. Despite the darkening global picture, despite the need to stay on top of the deficit, we'll do whatever it takes to return our economy to health. Whether driving cooperation abroad or pulling the right levers at home, as I said, a gear change for growth.

Thank you.

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