

Institution: Cardiff University
Unit of Assessment: 19 – Business and Management Studies
Title of case study: Influencing British macroeconomic policy and the relationship with the European Union in the aftermath of a global economic crisis
<p>1. Summary of the impact (indicative maximum 100 words)</p> <p>Following the global economic crisis of 2007, the question of how macroeconomic policies could be used to ameliorate its consequences has come to the fore. Research led by Professor Patrick Minford at Cardiff Business School (CBS) has promoted a shift in policy in the UK in a classical direction and away from the Keynesian demand management approach. CBS researchers from the Julian Hodge Institute of Applied Macroeconomics (JHIAM) have shown through economic modelling how a series of measures, for example, clear monetary rules which target inflation, could benefit the UK economy. The research has also been used both directly and indirectly, via MPs and intermediaries, to inform policy debates around such major issues as Britain's membership of the European Union (EU), as well as contributing to the wider public debate.</p>
<p>2. Underpinning research (indicative maximum 500 words)</p> <p>JHIAM is home to a group of researchers at CBS who have carried out modelling work on the UK and other economies. They consist primarily of Patrick Minford (Prof 93-present, joint-appointment with University of Liverpool 93-97), Kent Matthews (Prof 96-present), Mike Wickens (Prof 08-present), Vo Phuong Mai Le (PhD Student 04-08, Research Fellow 08-10), David Meenagh (Research Assistant 98-04, Research Associate 04-12, Lecturer 12-present) and Bruce Webb (Research Associate 95-12, Lecturer 12-present); others involved in various ways are mentioned in Section 4. The work of JHIAM has involved the building of economic models, originally the Liverpool Model of the UK^{3.1}, and later a variety of Dynamic Stochastic General Equilibrium (DSGE) models built on Rational Expectations and exploiting recent developments in macro-modelling^{3.2 & 3.3}. In this Rational Expectations approach which assumes that on average people in the economy make choices as if they understand how the economy works, demand effects are generally of at most temporary importance while supply-side policies have desirable permanent effects on the economy^{3.1}. As part of this endeavour new methods of estimating and evaluating models have been developed^{3.2} and the principles of the approach applied to the evaluation of macroeconomic policies^{3.1, 3.4 & 3.5}. These have included monetary and fiscal policy^{3.1 & 3.4}, exchange rate policy including the Exchange Rate Mechanism (ERM) and entry to the euro^{3.5}, and supply-side policy, including policy on employment, growth and the EU^{3.1 & 3.6}. The research has cumulatively added to the stock of evidence both on the (strong) empirical basis of this approach^{3.2 & 3.3} and on the detailed effects the embrace of these new policies would have^{3.1 & 3.3 - 3.6}.</p> <p>The need for a fiscal plan is a key implication of the group's models which embody expectations as the major channel through which monetary policy has its effects. As such, there needs to be an emphasis on limiting money supply growth to curb inflation and on ensuring that tax policy is then consistent with stabilising the level of public debt^{3.1 & 3.4}. As an important lever for stimulating foreign direct investment, economic growth and employment, policy in the field of taxation is one example of an area that researchers at JHIAM have recently revisited. Early work aimed at modelling the so-called 'Laffer effects' (the effects of lower marginal tax rates on the supply of work, effort and tax avoidance) provided the grounding for new calculations to be made. These identified several key reforms in tax policy which, together, could lead to substantial benefits to the UK economy. Among these reforms, proposed by Minford in 2006, was the abolition of the top rate of income tax, the revenue loss from which he demonstrated would be offset by broadening the base of taxation and by its positive effects on labour supply, innovation and productivity growth.</p> <p>In the early 2000s, with the argument for the UK to join the European Economic and Monetary Union strong, Minford and colleagues used economic models to investigate the extent to which the UK would suffer from losing its power to set its own independent interest rate through having its own currency and exchange rate. This work demonstrated that joining the euro would more than double the variability of the UK economy and led researchers to conclude that euro entry would be extremely damaging^{3.5}. JHIAM researchers have also evaluated the economic impacts on the UK of EU membership, which they have shown to carry significant net economic costs of a supply-side nature^{3.6}. Besides documenting the damaging effects of intrusive labour market regulations through</p>

their economic models of the UK, Minford and colleagues also investigated the less well-understood cost to the UK of the EU's protectionist trade policies in agriculture, manufacturing and services. Applying a standard model of UK, EU and Rest-of-the-World trade, Minford showed that through these policies, the EU is levying costs in wasted resources in the order of 3% of GDP.

3. References to the research (indicative maximum of six references)

1. **Matthews, K. and Minford, P.** (1996) British inflation and unemployment in the 1970s: a model-based decomposition, *Applied Economics*, 28 (1): 103-115. [10.1080/00036849600000013](https://doi.org/10.1080/00036849600000013)
2. Le, V.P.M., **Meenagh, D., Minford, P.** and **Wickens, M.** (2011) How much nominal rigidity is there in the US economy? Testing a New Keynesian DSGE Model using indirect inference, *Journal of Economic Dynamics and Control*, 35 (12): 2078-2104. [10.1016/j.jedc.2011.08.009](https://doi.org/10.1016/j.jedc.2011.08.009)
3. **Meenagh, D., Minford, P.**, Nowell, E. and Sofat, P. (2010) Can a real business cycle model without price and wage stickiness explain UK real exchange rate behaviour?, *Journal of International Money and Finance*, 29 (6): 1131-1150. [10.1016/j.jimonfin.2010.02.006](https://doi.org/10.1016/j.jimonfin.2010.02.006)
4. **Minford, P.**, Nowell, E. and **Webb, B.** (2003) Nominal contracting and monetary targets – drifting into indexation, *Economic Journal*, 113 (484): 65-100. [10.1111/1468-0297.00085](https://doi.org/10.1111/1468-0297.00085)
5. **Minford, P., Meenagh, D.** and **Webb, B.** (2004) Britain and EMU: Assessing the costs in macroeconomic variability, *The World Economy*, 27 (3): 301-358. [10.1111/j.1467-9701.2004.00602.x](https://doi.org/10.1111/j.1467-9701.2004.00602.x)
6. Book: **Minford, P.**, Mahambare, V. and Nowell, E. (2005) Should Britain leave the EU? An economic analysis of a troubled relationship, Edward Elgar Publishing Ltd. in association with the Institute of Economic Affairs. ISBN 978-1845423797. Copy available from HEI on request or online at: http://www.patrickminford.net/europe/book_index.html.

4. Details of the impact (indicative maximum 750 words)

Following the global economic crisis of 2007, there has been a particular focus both in the UK and Europe on how macroeconomic policies can be used to stimulate economic recovery. A separate, though closely related and interdependent issue faced by the international community is that of the euro-crisis. In this context, JHIAM's research provides not only an evidence-base for **policy makers** and the **business and financial community**, but a knowledge-base for **society**, which is ultimately bound by decisions made by the government.

Impact on public policy

The macroeconomic policy issues that align with JHIAM's research and have been the focus of debate since 2008 include: the budget deficit; the crisis in the euro-zone and the UK decision to stay out; monetary policy, including taxation and the inflation target; and growth and employment and the implications for these of EU membership. In all these areas of macroeconomic policy JHIAM researchers have contributed to policy debate, both **directly**, by giving evidence and acting in an advisory capacity to various government committees, and **indirectly**, through intermediaries and by providing an evidence-base for politicians to base their arguments on. A key example concerns the UK's role in Europe which has dominated politics since the Coalition government came to power, forcing policy makers to consider the economic impacts of EU membership.

The **direct contribution** of JHIAM researchers to policy debates include Minford's appearance in front of both the House of Lords EU Sub-Committee A on Economic and Social Affairs as part of the 'Euro Area Crisis: Follow-up Inquiry' (3 July 2012)^{5.1} and the House of Commons Foreign Affairs Committee at an inquiry into '[The Future of the EU: UK Government Policy](#)' (11 September 2012), where he was introduced by the Chair of the committee as "*one of the most prominent economists advocating British withdrawal from the EU*"^{5.2}; Minford went on to make direct reference to findings published in 3.5 and 3.6. For example, he referred to the "*considerable costs [of] being inside the European Union*" as a result of its "*protectionist*" nature and specifically to the "*3% of GDP*" that would be gained by "*moving to free trade*"; this led Members to question Minford further on the process and consequences of the UK exiting the EU^{5.2}. In the case of the House of Commons inquiry, the route to influence is visible through the scrutiny of on-going correspondence between Lord Boswell (Chair of the Committee) and the Financial Secretary (HM Treasury). A letter dated 24 July 2012, composed by Lord Boswell, includes direct reference to Minford's evidence which Boswell uses in support of questions he poses to the Financial Secretary, for example, relating to the "Compact for Growth and Jobs" and the importance of public opinion in the euro-crisis^{5.3}. Both these questions were subsequently addressed by Rt Hon Greg Clark MP (the

Financial Secretary at the time) in the government's response, issued on 3 October 2012^{5.3}.

JHIAM research also enters the political arena **indirectly** through its use by backbench MPs. According to a senior politician^{5.4}, Minford's team's "*comprehensive economic analysis of UK macroeconomic issues in an EU setting provides MPs, in particular those within groups such as 'Fresh Start' and 'Better Off Out' with valuable material to support their arguments.*" Members of the 'Better Off Out' campaign are keen to highlight research on the cost of EU membership. An article in The Commentator in which the group's Director, Rory Broomfield, states "*This burden of regulation ... is said to be 5 percent of UK GDP per year ... Similar estimations have been made by ... Professor Patrick Minford CBE*" ("[A referendum is only the start: We must plan for the finish](#)", 15 May 2013), demonstrates the use of Minford's research in supporting their argument.

JHIAM researchers also interact regularly with **intermediaries** in order to achieve indirect impact on policy and practice. A number of policy think-tanks benefit from JHIAM's research via publications and seminars, including the Adam Smith Institute, The Taxpayers Alliance, Reform, Open Europe and the Centre for Policy Studies. JHIAM's strongest relationship is with the **Institute of Economic Affairs** (IEA) whose mission is to communicate ideas about the workings of the market economy. The IEA claimed to reach an estimated 750 million people in 2012, influencing government through input to select committees and consultations, and the wider public through extensive media coverage. Several members of the JHIAM research team have contributed written material to the think-tank. For example, Minford has recently contributed to two IEA books. In the first, '[Sharper Axes, Lower Taxes](#)' (2011), a book which had a print run of 2,600 and has been downloaded over 4,590 times, Minford co-authored a chapter in which he explained the results of his taxation modelling. This book received endorsements from several MPs and others, including the following comment from Lord Lamont: '*I particularly enjoyed the chapter by Patrick Minford and Jiang Wang, which persuasively queries the idea that "state investment" contributes to higher economic growth*' (published on IEA [website](#))^{5.5}. In the second, '[The Euro – the Beginning, the Middle ... and the End?](#)' (2013), he wrote a chapter which drew heavily on JHIAM's research into the cost of the UK's membership of the EU, and concluded that "*the institutional evolution being triggered by the euro crisis threatens to make the [substantial net economic costs on the UK] higher still ...*" This report had a print run of 2,300 copies, has been downloaded over 1,724 times and was featured on Sky News, BBC 5 Live, BBC Radio 4, BBC Radio 2 and in a comment in The Daily Telegraph ("[Europe's leaders would do well to listen to some constructive criticism](#)", 11 April 2013). An earlier publication by Minford, '[Should Britain join the euro?](#)' (2002), also continues to be of value with over 400 downloads taking place from January to June 2013. [5.6]

Another key element of JHIAM researchers' strategy to achieve **wider influence** is through membership of the IEA sponsored **Shadow Monetary Policy Committee** (SMPC). The SMPC was founded in 1997 as a forum of independent monetary economists to debate monetary policies of the newly independent Bank of England. Minford (co-founder) and Matthews have been members since its inception. Prof. Akos Valentinyi and Wickens, both members of JHIAM, also belong to the SMPC alongside well-known City economists Peter Warburton, David B. Smith, John Greenwood (Invesco) and Trevor Williams (Lloyds TSB). The SMPC's monthly output (a freely available report on the monetary situation drawing on the research of its members) is widely cited in the media and followed by the Bank of England Monetary Policy Committee (MPC). [5.6]

Through pathways such as these, JHIAM's research has influenced and continues to **influence policy decisions**. Recent policy changes that are consistent with JHIAM's research include the Prime Minister's veto of any Treaty change at the EU summit in December 2011 and most recently his speech on EU renegotiation and an in/out referendum on 23 January 2013. The latter policy change was likely driven at least partly by pressure from backbenchers, with an article ("[Better off out?](#)", 17 January 2013) published by the think tank, The Centre for Policy Studies, in the run up to the announcement stating that "*the great majority of the Conservative party is clear that [Britain's relationship with the EU] should change ...*"; the same article credits Minford as one of the principal sources of ideas relating to the consequences of EU withdrawal.

Impact on the business and financial community

Researchers at JHIAM are committed to engaging politicians on issues critical to the business community in the UK. For example, in 2011, Minford played a lead role in a media campaign in respect of a letter, published in the Financial Times on 7 September, which warned that the 50

penalty tax rate was “*doing lasting damage to the UK economy*” due to the unfavourable economic environment for business which it created. The letter was signed by 20 UK economists, including representatives from eight universities and two former MPC members. The publishing of this plea not only led the Treasury to respond with a public statement in which it stated that the Chancellor had “*asked HMRC to conduct an analysis of the revenue raised by the rate*”, but also captured the attention of the media, with Minford invited to contribute to a [debate](#) on the issue hosted by Radio 5 Live. The support from academics on this issue enabled business leaders to launch similar campaigns of their own, with subsequent letters along similar lines being published in The Telegraph in November 2011 and February 2012. This debate culminated in the top 50 pence tax rate being cut in the 2012 Budget.

Impact on society

The contribution of JHIAM’s research to policy makers and the financial sector is complemented by its cultural value and input to wider public debate around economic policy^{5.7-5.10}. Minford is a regular contributor to BBC Radio 4 current affairs programmes, notably Today, on which, in the context of his research, he has provided insights into topics such as inflation targeting ([Is the BoE wrong on inflation?](#), 18 October 2011), exchange rate and finance ([Are financial markets rational?](#) 20 March 2010). Minford was also invited to contribute to the Radio 4 series [Stephanomics](#) (31 July 2012) in an episode which looked at whether growth should be a major target of government policy^{5.7}. [text removed for publication]

5. Sources to corroborate the impact (indicative maximum of 10 references)

1. Oral Evidence from the House of Lords EU Sub-Committee A on Economic and Social Affairs inquiry: ‘Euro Area Crisis: Follow-up Inquiry’ (3 July 2012), available at: <http://www.parliament.uk/documents/lords-committees/eu-sub-com-a/EuroCrisis/EACFUSuppandoral.pdf>. Minford’s contribution can be found on p33-54.
2. Transcript of oral evidence by Minford to the House of Commons Foreign Affairs Committee inquiry into ‘The Future of the EU: UK Government Policy’ (11 Sep 2012), available at: <http://www.publications.parliament.uk/pa/cm201213/cmselect/cmfaaff/c115-iii/c11501.htm>.
3. Correspondence following the House of Lords EU Sub-Committee A on Economic and Social Affairs inquiry into ‘Euro Area Crisis: Follow-up Inquiry’ (see 5.1) in which Minford’s evidence is used in support of questions posed in Letter 1 (24 July 2012) on pages 3-5. These questions were subsequently addressed in Letter 2 (3 October 2012). Both available at: <http://www.parliament.uk/documents/lords-committees/eu-sub-com-a/EACJan2013/Combinedresponse.pdf>
4. Statement: Member of Parliament, corroborating Minford's contribution to the policy debate surrounding the UK's membership of the EU.
5. Endorsements of the ‘Sharper Axes, Lower Taxes’ book which demonstrate the value to MPs and others of this publication. See the Institute of Economic Affairs website at: <http://www.iea.org.uk/publications/research/sharper-axes-lower-taxes>.
6. Contact: Editorial Director, Institute of Economic Affairs (IEA), to corroborate the influence of JHIAM’s research on policy makers and wider society via the IEA and the SMPC.
7. Minford interviewed by Stephanie Flanders about how far long-term economic growth should be the over-riding objective of governments in countries like Britain. Radio 4, 31 July 2012, Stephanomics, Series 2, Episode 3. Available at: <http://www.bbc.co.uk/programmes/b0117sf9>
8. Minford contributed to a news feature about banking regulation. BBC News Channel: 19 Sep 2008, Viewpoints: Where now for capitalism? Available at: <http://news.bbc.co.uk/1/hi/business/7621771.stm>
9. Minford contributed to a news feature about interest rates. BBC News Channel: 4 Sep 2008, Grim backdrop to UK rate decision. Available at: <http://news.bbc.co.uk/1/hi/business/7596695.stm>
10. [text removed for publication]

All documents and web pages were saved as pdf on or before 26.07.13 and are available on request from the HEI.