



Newsletter

November 2009

*The **Social Market Foundation** is an independent public policy think-tank, developing and advancing innovative solutions across a broad range of economic and social policy. We publish original research, hold seminars and debates in Westminster and beyond, and run a diverse programme of events at the three main party conferences.*

Since its foundation in 1989, the work of the SMF has been principally devoted to promoting the social market philosophy, which seeks to marry markets and social justice. It neither sees the market as a necessary evil nor as an end in itself but as a means to improve people's lives. It is underpinned by adherence to two key principles: first, a positive preference for market mechanisms, while recognising that a truly pro-market approach is often not a free-market one; and second, a belief that a sustainable market economy rests on social and political foundations that are widely regarded as fair. Our work aims to elucidate these ideas and to explain why the social market is a fruitful source of solutions to public policy problems.

For further information please contact the editor, Laura Tomlinson at ltomlinson@smf.co.uk

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Social Market Foundation

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Welcome to the November edition of the SMF newsletter

The final parliamentary session that starts next week will be addressing big issues in the little time that remains before the general election. "The size, scope and role of the state is of course the scene of a vigorous political debate," said David Cameron this week, in his speech on poverty. Philosophical differences between the parties are now centre stage in a way they have not been for years, and politics is the better for it.

The Financial Services and Business Bill, to be unveiled next week, will see Government and Opposition debating the most important regulatory agenda for years. Those interested in these arguments should join us for the next of the SMF's New Finance series of events, where Gavyn Davies and John Kay will join us to discuss the idea of 'socially useless' banking and what to do about it.

Among other bills likely to feature in the Queen's Speech are those addressing energy, and flooding and water management that raise important questions about where the boundaries of governmental and corporate responsibility lie. Supporters of the proposed Equality Bill argue it addresses blatant inequalities in opportunity, treatment and pay. Opponents counter that it places an unnecessary burden on business, amounts to social engineering and may be counter productive. Meanwhile, the Schools Bill will see Labour put forward its ideas for improving schools with the Conservatives countering that increasing the range of providers of state education and liberalising supply is the only real key to achieve progress. Interesting times ahead.

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Latest news

New multi-media website

After a highly successful conference season it is back to Westminster for all of us here at the SMF. But for those of you who missed out on the action in Bournemouth, Brighton and Manchester check out our newly updated website, complete with video highlights and Podcasts from the party conferences www.smf.co.uk

SMF gives evidence to the Health Committee

On the 5th of November James Lloyd, Senior Research Fellow at the SMF, gave evidence to the House of Commons Health Committee on social care.

Following the publication of the Green Paper Shaping the Future of Care Together, the Health Committee is undertaking an inquiry into the future of social care services.

The inquiry is looking at options for:

- future funding of long-term residential and domiciliary care for older people and people with physical or learning disabilities;
- personalisation of social care services;
- more effective, consistent and user-friendly social care services.

Job Opportunities at the SMF

The SMF is looking to add to our successful team with a new Finance and Operations Manager and a Conference Manager. These exciting and challenging roles are central to our work.

For more details please visit the [Job Opportunities](#) section of the SMF website

Westminster boardroom

The conference room at the Social Market Foundation is available to hire for meetings and seminars. It is an ideal venue for those seeking a location near the heart of government, as we are situated within a short walking distance of underground stations at Westminster, St James' Park and Victoria and just minutes from the Houses of Parliament and Whitehall.

For more information about how to book our boardroom and hire rates please contact SMF on 020 7222 7060 or see our website www.smf.co.uk/room-hire

Note from the Director

Ian Mulheirn
Director



“securitisation appears to have been profitable only because buyers were somehow cajoled into paying a *premium* to the bankers who made it all so confusing”

Many influential figures have described recent financial innovation that lay behind the banking crisis as ‘socially useless’. But what does it really mean and what should policymakers do about it?

Given the causal role of recent financial innovation in the biggest financial crash since the 1930s, it might seem like an understatement to conclude that some of that innovation has been socially useless. Nevertheless, as a viewpoint held by well-respected observers including Lord Turner and Vince Cable, it represents a remarkable and rapid sea-change in mainstream opinion about financial services over the past year. But in order to think about policy implications, we need to pin down what it means to say that financial innovation was socially useless.

For the past 30 years, the prevailing economic orthodoxy gave intellectual cover for policymakers to keep their noses out of the City’s activities. In this perfect world of economic man and economic woman, only a minimal role for policymakers and regulators remained, since markets were, by assumption, self-correcting.

Seen in this context, the justification for why the free market was creating social value came in two parts. First, it was thought that the new products of financial innovation must be *economically* valuable, since otherwise there wouldn’t be a buyer and a seller willing to trade them for mutual gain. Second, having established the economic value of financial products, proponents argued that they must also be *socially* valuable since they apparently increased society’s overall wealth. Both steps in this argument are flawed.

On the first point, it is clearly not true that trade in many fancy financial products was ultimately for mutual gain. The fact that there were buyers for various asset-backed securities – bundles of debt that were chopped up, mixed around and sold on – was clearly not, in itself, evidence of their economic value. Once the crisis struck, investors realised they were holding assets worth a lot less than they had thought. In other markets where a buyer can’t easily assess the real value of their purchase (think of second-hand cars), they usually demand a *discount* for the associated uncertainty. By contrast, securitisation appears to have been profitable only because buyers were somehow cajoled into paying a *premium* to the bankers who made it all so confusing.

On the second point, even where products are of economic value, as is the case with more conventional banking activities, it’s time we questioned whether that economic value necessarily equates to social value. Goldman Sachs’s CEO implausibly claimed at the weekend that bankers are ‘doing God’s work’. In the same week it was announced that the average Goldman employee’s remuneration would top £420,000 this year. But aside from the

revelation that doing God's work can be so lucrative, it's hard to see how even the economically valuable activities Goldman and others are now involved in can be socially valuable under current arrangements. Goldman's profits are at least partly the product of monopoly power in a market that has become even more concentrated after the banking sector carnage of the past 14 months. Their activities are also underwritten by taxpayers' implicit guarantee to bail the bank out should disaster strike again. The economic value of their work is insufficient proof of its social value when the distribution of the spoils and the risks is so artificially skewed.

So while conventional banking activities are an essential activity for a prosperous society, equating profit-making with social value-creation is no longer a no-brainer for a variety of reasons. In policing activities of financial markets, policymakers and regulators must in future avoid being seduced by the notion that people are omniscient in their understanding of financial risks. But secondly, re-establishing the link between economic and social value is vital to sustaining the legitimacy of the market economy. To achieve that, policymakers need to start worrying about who benefits from banking and whether it is fair.

The next debate in the SMF's New Finance seminar series, entitled Socially Useless? Financial Innovation and the Real Economy will take place on 26 November. Speakers include Gavyn Davies and John Kay.

Forthcoming Publications

How to Make Fiscal Policy – The Option and Choices

James Lloyd and Ian Mulheirn

This discussion paper explores institutional choices around how fiscal policy is formulated, identifying the relevant trade-offs and proposing a bold new approach for the next decade.

For more information please contact James Lloyd on jilloyd@smf.co.uk or 0207 227 4411.

Strategic Commissioning

Barney Gough and Ian Mulheirn

The gaping hole in the public finances means that the government must get more bang for their buck when it comes to delivering public services. For the next decade the most urgent public policy question will be: how can public services achieve more for less?

When governments across the developed world faced a similar question in the 1970s there was a shift away from state delivery, which was seen to be inefficient. Market-style disciplines became key tenets of public service reform in the UK and across the world.

More recently the personalisation agenda has been introduced in an attempt to put the citizen at the centre of public service delivery and to further improve quality and efficiency.

However, these reforms have not been introduced in a strategic manner. They have been piecemeal and sporadic. A coherent framework that attempts to assess the level at which a service should be commissioned is lacking. This paper sets out such a guide for policymakers.

Public services should be commissioned and controlled by the user whenever possible, but there are a number of factors that mean it is not always appropriate for individuals to commission their own services. This paper explores these factors and provides policymakers with a guide to the level at which different services should be commissioned.

For more information please contact Barney Gough on bgough@smf.co.uk or 0207 227 4403.

Kindly supported by the Learning and Skills Council and Avail.

Creating Social Capital

Dr Sandra Gruescu and Verena Menne

Migration to Britain has been rising over the last decade, and is set to rise further in the future. Whilst a free market approach would focus on migration to support labour market efficiency, a social market approach takes the social repercussions of a mobile society into account and sees a role for the state to cushion negative effects.

This SMF research project analyses the circumstances under which people with different histories, nationalities and ethnicities get together and build networks. The report assesses the role community organisations can play in helping shape networks and what the state should do to support them.

The research is based on interviews conducted with community leaders in London, Birmingham, Madrid and New York, from which insights into the emergence of 'bridging social capital' are drawn. The findings from these interviews, as well as the role of government in the promotion of bridging social capital, were discussed at an expert seminar.

The report will be launched in January. For further questions, please contact the project leader, Dr Sandra Gruescu at sgruescu@smf.co.uk.

Kindly supported by Barrow Cadbury Trust.

Forthcoming Events

Increasing Take-up of Child Trust Funds among Low-Income Households

Date: Wednesday 25th November 2009, 08.45-10.00
 Venue: Social Market Foundation, 11 Tufton Street, London SW1P 3QB
 Chair: Ian Mulheirn, SMF
 Speakers: Dr Rajiv Prabhakar, London School of Economics and the Open University
 Brian Pomeroy CBE, Chair, Financial Inclusion Task Force

The recent announcement that under a Conservative government Child Trust Funds would be restricted to families earning less than £16,000 per year puts pressure on the scheme to demonstrate its value in the context of a dire situation for public spending.

Child Trust Funds (CTFs) are tax-free savings accounts for children born after September 2002, which were designed to encourage saving, increase financial capability, and unlock other benefits identified by the asset-based welfare agenda. Children are able to access the funds built up in a CTF from the age of 18. As well as being encouraged to make ongoing contributions into a CTF, parents are expected to open a CTF for their new-born child, choose an account-type and a provider.

However, rates of take-up for CTFs have varied. On average, 26% of parents do not open a CTF, and this figure is higher among lower socio-economic groups. Indeed, the lack of parental engagement among the most deprived groups has been a significant stumbling block for the CTF scheme.

This seminar will therefore explore the ways in which behavioural economics theory may both explain non take-up of CTFs by parents, and provide potential pointers toward increasing parental engagement. The seminar will explore issues of inertia, advice and information, and draw upon focus groups with parents that explored barriers to the usage of CTFs.

Key Questions:

- What insights can behavioural economics provide for explaining problems of parental engagement with CTFs?
- Can solutions derived from behavioural economics and applied to other problems of financial behaviour be used to increase engagement with CTFs, such as 'choice framing'?

This event is kindly supported by the Economic and Social Research Council

If you would interested in taking part in this seminar please email events@smf.co.uk to reserve a space or telephone 020 7222 7060.

New Finance Debate – Socially Useless? Financial Innovation and the Real Economy

Date: Thursday 26th November 2009, 17.30 – 19.00
Venue: Social Market Foundation, 11 Tufton Street, SW1P 3QB
Chair: Ian Mulheim, SMF
Speakers: John Kay, Financial Times
Anthony Belchambers, Chief Executive, Futures and Options Association
Gavyn Davies, Chairman of Fulcrum Asset Management, former Chief Economist, Goldman Sachs

It would have been inconceivable even six months ago, but the following statement is now true: the CEO of Goldman Sachs and the Chairman of the FSA are united in believing that much banking activity of the last decade was socially useless.

Lending and deposit taking by banks - credit intermediation - is clearly essential for the functioning of the economy. But in the analysis of the credit bubble that exploded in 2007, a growing number of stakeholders across the banking sector now believe that a significant proportion of the activities of major banking institutions make negligible or limited contribution to the "real economy".

This change in the debate is significant, creating as it does more space for policymakers to act. However, while recognition of "socially useless" banking is growing, uncertainty still clouds what exactly is socially useful banking, how this can be categorised, identified and measured, and what all of this means for practical regulation.

This debate will therefore explore the questions:

- What is socially useful banking and what is socially useless?
- Is socially useless banking the same as economically useless?
- What exactly are the negative externalities associated with socially useless banking activities? How can they be measured and how can the costs and benefits of such activities for society be evaluated by regulators?
- Does banking activity have to be "socially useful" to be valid and permissible?
- Should regulators worried about the existence and effects of socially useless banking consider radical measures to reduce its prevalence, such as a Tobin tax?

This event is free and open to all; however registration is required. If you would like to attend this event, please email events@smf.co.uk or call 020 7222 7060. Please note that places at this event are strictly limited.

Articles



School lotteries strike back

David Furness

Do parents cheat the system to get children into good schools? The Office of the Schools Adjudicator says yes, and will conduct further work on the issue of misleading applications. However the solution to cheating isn't to toughen up the existing rules, but to accept that the whole system of catchment areas inherently disadvantages poorer children. Policymakers should revisit the idea of admissions through ballot – school lotteries strike back.

A report last week commissioned by Schools Secretary Ed Balls found that some parents flout the rules by pretending to live in the catchment area of their preferred school. While the majority are honest about where they live, some parents obtain by deception a school place for their child that should rightfully have gone to someone else. The situation is sufficiently serious that some local authorities have asked for extended powers to prosecute parents who abuse the system.

It is tempting to place the blame squarely on parents who lie to get their child into their favoured school. It is clearly wrong to rent temporarily a property within a particular catchment area or to use a relative's address on an application form. But as with the furore over MPs expenses we should not be shocked that when presented with a set of rules, individuals do all they can to extract maximum benefit for themselves. Ed Balls has commented that "It's really important that parents who are properly playing by the rules aren't disadvantaged by some parents who break the rules or provide false information. That's not fair." Of course it's not fair. But it's the reality of a rules based system and is unlikely to change whatever the legal sanction available to local authorities.

School places should no longer be based on catchment areas. The emphasis on where you live firstly provides an incentive for parents to 'game' the system (as last week's report makes clear) and secondly reinforces social divisions as children from deprived areas are denied access to the schools favoured by their wealthier counterparts. Instead, the use of lotteries to allocate school places should be extended, giving poorer pupils an equal chance of securing a place in a high performing school regardless of where their family can afford to live.

In a review of the use of school lotteries earlier this autumn the Schools Secretary was told that their impact is highly limited: "in the large majority of cases it is used only as a tie-breaker to allocate final places and therefore has very little impact on the allocation of school places in general". This must change. As the SMF suggested as far back as 2004, parents should be given a free choice of school, with oversubscribed schools using ballots to determine who gets a place, without regard to catchment areas that artificially inflate house prices to the

“the use of lotteries to allocate school places should be extended”

detriment of poorer families. Ballots cannot be influenced by pushy parents, and are a wholly fair way of determining which children get into the most popular schools.

The only real objection to the extension of lotteries into school admissions is a political one. The Office of the School Adjudicator's report found that few Local Authorities will adopt a ballot based system because of its high negative media profile. Richer parents are terrified of change to a system that benefits them to the detriment of poorer, less articulate, parents. One parent writing on a Times blog argued that "Parents have the right to do everything they can to further their child's interests." This is fundamentally antisocial. Parents, just like everybody else, have a wider responsibility than just to their own child. This should include recognition that manipulating a catchment based admissions system is unfair and harmful to the rest of society.

It is time for politicians to accept that parental choice of school should be for the many, not the few. Allowing parents to choose any school they wish, regardless of where they live, is the fairest way of evening up educational access and giving all children access to the best possible education. It is time for school lotteries to strike back against an admissions system that favours the rich over the poor and the unscrupulous over those who play fair.

To view the SMF's report on school lotteries please go to <http://www.smf.co.uk/school-admissions.html>



Finding the Path to Economic Recovery

Rt Hon Theresa May MP

We start off with the view that work is the best route out of poverty, that those people who are able to be in work should be in work, and a recognition that work is not only good for our economy, but good for society and individuals too. So how are we going to tackle the issue of people who are currently becoming unemployed as a result of the recession as well as helping those who were out of work or on incapacity benefit before that? Some of those people claiming incapacity benefit won't be able to get into the workplace. But a lot of people on incapacity benefit, who over the last twelve years have been pushed to one side and forgotten, are capable of being in work and want to be in work too.

We propose a single Work Programme which will cover people who are recently unemployed, notably young people who have become unemployed, and crucially will include those people on incapacity benefits. This single programme will replace a multiplicity of programmes and make the most of expertise in private sector and voluntary organisations. It will enable those private and voluntary sector welfare to work providers to make an assessment about the needs of the individuals they are dealing with and how they can help get them back into the workplace. This is far preferable than saying to people, 'well you're on this benefit, therefore you must need this sort of programme'. It pays providers by results, telling them that we want you to be focused on getting people into jobs.

“work is not only good for our economy, but good for society and individuals too”

We recognise that during the recession that task is harder; there are fewer job vacancies. So we will give people a longer opportunity to get people into work - the period of engagement with an individual would probably be two years rather than the one year it is at the moment. But the focus will remain that the provider gets the payment when somebody has found a job. And we will define a sustainable job not as thirteen or twenty six weeks as the government does but a full year. Holding a job for a year really shows that people are in the workforce, and that it is making a difference to their lives, and giving them some hope for the future.

Crucially, we will also pay the providers a different fee according to how hard it is going to be to place someone in the workplace. At the moment they just get one fee for everybody, and that means that the people who are easy to get into the workplace are dealt with. They are creamed off. The people who are harder to get into the workplace are left behind and we will change this.

These proposals will make a real difference in terms of the number of people who are helped back into jobs and will also benefit wider society and the economy. We will use the savings from the benefit bill of getting people into employment to pay for the programmes to help get them there – using the DEL/AME split to achieve this.

So the single Work Programme we propose deals with more people because it deals with people on incapacity benefit. It offers a whole new range of options for welfare to work providers in terms of extra apprenticeships, training opportunities, and work-pairings with sole traders. It will get rid of the bureaucracy and the programme complexity that we have at the moment and be focused absolutely clearly on getting people into jobs, and paying the providers by the results of getting people into sustainable work. I think that will make a very real difference to people's lives, and in doing so make a real difference to the economy.

This article is a transcript of Theresa May's speech to the SMF keynote event at the Conservative Party Conference 2009. Joining her on the platform were Oliver Letwin MP, Brendan Barber of the TUC and Margot James, Conservative PPC for Stourbridge.

To view our latest welfare to work publication please go to
http://www.smf.co.uk/vicious_cycles.html

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