NewStatesman

Ensuring ongoing competitiveness

Enabling UK companies to fulfil their potential

with

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In association with

GM

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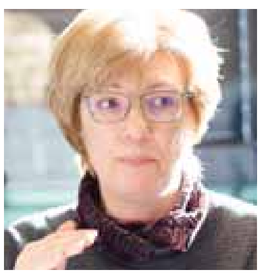

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Up for debate: how do you create the right environment to allow business to flourish?

It's competition time

Improving a nation's productivity requires a complex blend of nudges and interventions. **Jon Bernstein** listens to leading figures make the case for industry

Here's a question that has challenged successive governments: how do you create the right environment to let business thrive domestically and internationally? And a supplementary – what are the right policy levers to pull that balance the needs of the business, its workforce, the economy and society at large?

Given that the UK boasts the world's fifth-largest economy but is tenth and falling in the World Economic Forum's competitiveness ratings, it seems reasonable to suggest that the present industrial policy framework is imperfect. A recent survey by the manufacturers' association EEF found a 14 per cent drop in respondents who view Britain as a competitive manufacturing base.

In an effort to address these issues, the *New Statesman* – in association with General Motors UK – brought together leading policymakers and influencers, industry and academia to discuss the obstacles and opportunities. The round table, entitled "Ensuring Ongoing Competitiveness: Enabling UK Companies to Fulfil Their Potential", was held two days before George Osborne's March Budget. On the agenda were a wide range of topics, including the apprenticeship levy, the demise of an industrial strategy, effective energy policy, business rates and what the competitive landscape of the future will look like.

Apprenticeship levy

Kevin Brennan MP, the shadow minister for trade, investment and intellectual property, kicked off the debate and his ▶

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attention soon turned to the government's apprenticeship levy, a 0.5 per cent charge on payroll that comes into effect from April 2017. The levy will apply to employers with an annual pay bill in excess of £3m and Brennan is broadly supportive of the initiative.

"In principle it's a good idea," he said. "It's always been a good idea to have some kind of levy if it's properly thought through and administered. One of the great market dysfunctions about training is that the good guys do it and the bad guys don't do it – and the bad guys end up picking up the good guys' activities. That's the purpose of the levy."

Brennan argued that when the government announced the idea in last summer's Budget it was "not yet oven-ready" and warned that if it simply becomes "a burdensome tax on business as a way of transferring responsibility away from government . . . then that's a problem".

According to Helen Foord, manager of government relations at General Motors UK and Ireland, the apprenticeship levy would be a significant additional cost on top of her company's own training scheme. "We welcome the levy but the devil is in the detail," she said.

For Ann Francke, chief executive of the Chartered Management Institute, however, the case for the levy was clear. "The UK invests far less in training than its European counterparts, and its management and leadership rank below its counterparts'. The apprenticeship levy is designed in part to address that."

Francke (*facing page*) pointed to support among her membership and to CMI research suggesting that 72 per cent of parents support government plans. In the same survey, 61 per cent of parents said that they would rather their child took a degree apprenticeship with a major company than an Oxbridge degree. "If companies need to work harder in training their workforce in these high-quality areas such as engineering, they will reap the rewards," she said. "The good guys do it anyway. And they do it for a reason: it boosts their business and they know that."

Devolution and the levy

David Bailey, professor of industry at Aston University, suggested that devolution might provide a way of making the levy more palatable for organisations. "A lot of businesses think of the levy as . . . another tax coming from government. They might be a bit more supportive of it if the levy were retained locally and the businesses could have some say over how it's spent and invested."

Bailey added: "We are only going to tackle apprenticeships if we incentivise the big players like General Motors, Rolls-Royce and Jaguar Land Rover to massively overtrain, as they do in Germany, and then release those apprentices they don't want into the supply chain."

"Business rates is a colour-blind tax. You pay if you're in the red or in the black"

Business rates

The opportunities presented by devolution were invoked again when the discussion turned to business rates. For Foord and General Motors, business rates remain an area of contention. Specifically, she pointed to the way plant and machinery cost calculations were acting as a disincentive to instal energy-saving equipment. "We looked at putting photovoltaic cells in our Ellesmere Port plant [but] the impact on business rates meant that the initiative didn't happen," Foord said. She added that attempts to bring Polish suppliers into the same factory to improve production-line efficiency also proved prohibitive.

According to GM's own figures, the UK accounts for just 8 per cent of its European footprint but attracts 60 per cent of its property tax bill.

In the March Budget, Osborne made two concessions to those who have argued that business rates need amending. First he announced that 600,000 small businesses, many of them retailers, would be taken out of the tax altogether. Second, he would shift the measure of inflation for business rates from RPI (retail prices index) to the generally lower CPI (consumer prices index) from 2020.

However, the Chancellor failed to address the plant and machinery issue affecting bigger organisations. According to Chris Sanger, global head of tax policy at EY, the UK has the highest property taxes in Europe, while "manufacturers pay a much higher proportion of the overall business rates burden than their greater value added would suggest they should. There's a real distortion around the tax system." On the other hand, the country offers the most competitive corporation tax in Europe. Sanger (*pictured left*) conceded that was a great success for the UK but countered: "Business rates is a colour-blind tax. You pay it whether you are in the red or in the black."

Rob Fontana-Reval, head of tax and fiscal policy at the employers' association, the CBI, agreed: "The common factor is that it is a growing burden. It's a fixed cost regardless of whether you make a profit and is uncompetitive compared to the rest of the world."

Northern Powerhouse?

The director of the ResPublica think tank, Phillip Blond, suggested that large manufacturers were missing a trick. "Devolution is the pathway to go down," Blond said. "It's a door that's already open." The Localism Act, introduced during the last parliament, would allow for reliefs on a sectorial and geographical basis. "I think the government is open to the idea of piloting a completely new model for business-rate reliefs on a city region level."

Blond pointed out how the distribution of manufacturing in the UK skews to the north and that a competitive business rates policy on a regional basis could make the Northern Powerhouse – heralded by Osborne since 2010 – a reality.

In his March Budget, the Chancellor announced that from next April Manchester, Liverpool and London would all retain revenues from business rates in full to fund local services. He also announced plans for new mayors in greater Lincolnshire, East Anglia, the West Midlands and the west of England.

Chris Sanger and Helen Foord cast some doubt on Blond's suggestion, arguing that

Europe would interpret rate reliefs as state aid, something the government was aware of when drawing up devolved powers. "This is where someone needs to press," countered Blond. "Often when people say 'state aid' they stop and give up. If it's a matter of government policy that a whole regime of rates is devolved and that city regions take an entirely different approach to their own business topography, then you're in a different place than sectorial state aid issues."

Industrial strategy redux

Since the Conservative Party's outright victory in last May's general election, the Business Secretary, Sajid Javid, has talked of an "industrial approach", eschewing the usual construction – an "industrial strategy". Round-table participants argued that this was more than a semantic shift, marking a definite move away from the approach of Javid's Liberal Democrat predecessor, Vince Cable, and Labour's Peter Mandelson.

Some, including Labour's Kevin Brennan, felt this was a mistake. "It's disappointing that after the election the government started to shy away from even using the term 'industrial strategy'," Brennan said. "We felt that a consensus had built up, after what had happened in 2008 . . . we needed to rebalance our economy away from an over-reliance on the financial sector and more towards making things again."

Others agreed. "Industrial policy isn't picking winners," said Bailey. "That got us the Austin Allegro. Industrial strategy is a process of discovery between government and industry, identifying challenges and opportunities and then overcoming those. And it is about providing certainty . . . China has got a ten-year strategy on Manufacturing 4.0 – it thinks it will lead to the re-creation of small-scale manufacturing in quite a big way."

Marcelino Castrillo, managing director of business banking at RBS, added: "I don't think it's government's responsibility to decide which industries will be around in ten years, but it has a part to play in how you train the people who will transfer the knowledge and innovate in this country."

Energy and the environment

Successive governments have introduced initiatives and programmes designed to incentivise energy-saving. Yet for energy-intensive manufacturing operations these schemes can hamper competitiveness, especially when up against competitors in emerging markets. George Osborne appeared to agree – at least up to a point – when he made his announcement about the Carbon Reduction Commitment (CRC) energy efficiency scheme during the Budget. "It's not a commitment; it's a tax," he said. "So I can tell the House: we're not going to reform it. Instead, I have decided to abolish it altogether."

In a note on its website, the Treasury acknowledged business concerns that the carbon reduction scheme was "overly complex, administratively burdensome and ineffective". The CRC will be abolished from the end of 2018-19 and the Treasury will instead increase the main rates of the CCL (the climate change levy) to "cover the cost of the CRC abolition in a fiscally neutral reform".

Speaking before Osborne's Budget announcement, Alison Mungall, compliance

"If companies work harder training their workforce they will reap the rewards"

director of Carbon Credentials – an independent energy consultancy – said complexity of energy policy obliged organisations to spend far too much time complying and not enough time on the core purpose of improving energy efficiency and performance.

However, she added: "I know CRC gets a lot of stick but there were two things that were very good about CRC that shouldn't get lost. First, before it, nobody measured and monitored what their energy was; so, therefore how could you reduce it when you didn't know how much you were using?

"Second, there was the provision that it had to be signed off by a director or equivalent. That's been very successful in getting this issue into the boardroom that was previously dealt with by an accounts department."

Bailey also said: "There is an argument for high carbon prices so that it forces us to shift to a more sustainable development pattern. That needs to be done in a simple way but we also need to find ways to compensate manufacturers for those higher costs – and we've not done that."

Complexity and uncertainty

The obstacles extend beyond energy policy. A pre-Budget survey by EY found that complexity and uncertainty were the two most important inhibitors stopping businesses investing in the UK. Chris Sanger cited the Annual Investment Allowance as an example: "It's otherwise known as the 'yo-yo' allowance, because it's been up and down so many times."

Richard Bruges, chief executive of Productiv Group, a Midlands-based engineering firm, said consistent policy was "really important, particularly in an industry like automotive that has such a long gestation period". He cited a project he is working on that won't go into production until 2022 at the earliest. Consistency, he said, is an "enabler".

Both Tim Curtis, managing director of Ricardo Energy and Environment, and Kevin Brennan suggested that adversarial Westminster politics might play a part in a lack of consistency. "Governments do love to undo each other's policies and that can be very difficult for businesses to understand," Curtis said. Brennan added: "There is a danger that in wishing to change policies – as government's often do – the government ends up reinventing them under a different name."

Future strategy

Lee Hopley, chief economist at EEF, warned that stability only gets the UK so far. "We're really good at providing some levels of consistency but it's compromised and mediocre," she said. "And that's where we'll be in five years' time if we're not thinking about the kinds of business models, the kinds of technology that ▶

manufacturers are going to be using [especially if we] still have a capital allowance system that isn't an incentive and is rooted in the 1970s when the technology is 21st-century."

So, what will the landscape look like in five years? "Remanufacturing, service-oriented business models, the Internet of Things, big data. If you stack the bits of the tax system – business rates, capital allowances, energy taxation – up against that, it looks woefully out of date."

Hopley recommended a cross-government approach to industrial strategy. "If you did that, then decisions about things like business rates would be absolute no-brainers. You wouldn't include plant and machinery because the future shape of industry would dictate that that was not the right thing to do."

Dustin Benton, head of energy and resources at Green Alliance, expressed a similar view, arguing that a discussion around tax policy was "a zero-sum game". Instead, he suggested, that organisations should be developing their own industrial strategies to excite customers but also to reflect the changing nature of competition.

"If I think about how a European manufacturer is going to be competitive in the future, it's not going to be competing on labour costs and it's not going be competing on low tax rates," Benton said. "We've got expensive societies and we've got expensive infrastructures. Where we will be competitive is either by inventing some new, exciting product of the future, or we've done something to reduce the input costs radically."

Benton said that in five or ten years' time, previously prohibitively expensive renewables would be cheaper than fossil fuels. "Similarly, electric vehicles are going to be cheaper than fossil vehicles in probably a decade's time.

"The question is how do we get there? And how do we ensure that the UK and European manufacturers have a slice in that game? The emerging markets want the same stuff that we have but they can't afford to pay as much as we did. Hopefully if we can make things at much lower input costs we can sell them low-carbon, wonderful stuff."

Ian Allen, manager of regulatory affairs and CSR at General Motors, agreed that the potential of low-emission vehicles was exciting but cautioned against over-optimism unless governments could offer certainty. "We need that continuous commitment in terms of incentives. Yes, advances in technology may mean that in ten years time electric vehicles may be as cheap as internal combustion vehicles but they're not at the moment. It's a market push rather than a market pull."

He offered the example of hydrogen vehicles. "We got to the stage that the next step was commercial production but the timing wasn't right. The infrastructure to support hydrogen vehicles wasn't there and neither was the market for the cost of the vehicle."

National Living Wage

For the CBI's Rob Fontana-Reval, one of the biggest inhibitors was what he described as "the cumulative burden of business" since the election. "There has been a series of measures that taking each in turn you might agree and disagree on their merits – the National Living Wage, apprenticeship levy and so on – but what's definitely the case is that all of those things represent a cost on business which adds up," he said.

"We've calculated that inaction on business rates, National Living Wage and the apprenticeship levy adds up to about £29bn across the parliament."

On the National Living Wage, Fontana-Reval said: "We don't feel that mandating price increases or wage increases is the best way forward. We share a common ambition with the government in wanting to see wage rises – particularly as we've seen quite low levels of wage growth recently – but the key to growing wages is productivity.

"If businesses are not becoming more productive, it's difficult for them to pay their workers more without it just becoming something that adds to the cost ledger."

"Ensuring Ongoing Competitiveness: Enabling UK Companies to Fulfil Their Potential", a New Statesman round-table discussion, in association with General Motors UK, took place on 14 March 2016 at Portcullis House, Westminster.

So what is competitiveness, anyway?

"Competitiveness" is one of those words that's open to interpretation, malleable to the point of meaninglessness. The World Economic Forum offers the 12 pillars of competitiveness and this definition: "Competitiveness is the set of institutions, policies and factors that determine the level of productivity of a country." Those 12 pillars are:

1. Institutions
This is the legal and administrative framework within which individuals, firms and governments interact.

2. Infrastructure
Covers transport, energy supplies and telecommunications. Should be extensive, efficient and well developed.

3. Macroeconomic environment
High inflation and interest rates and fiscal deficits are the enemy of competitiveness.

4. Health and primary education
A fit, literate and numerate workforce is vital to a country's productivity.

5. Higher education and training
Required to create a workforce capable of carrying out complex tasks and adaptable to the demands of a globalised economy.

6. Goods market efficiency
Efficient firms producing goods demanded by the market should thrive.

7. Labour market efficiency
A flexible workforce, wage fluctuations, workplace equality and employee incentives mean efficient labour markets.

8. Financial market development
Vital to channel resources to entrepreneurial projects with prospects of the highest return.

9. Technological readiness
To enhance the productivity of daily activities and production processes.

10. Market size
Trade, as a substitute for domestic demand, should have a positive effect on growth.

11. Business sophistication
Quality of business networks and of a firm's operations and strategies.

12. Innovation
Needn't be technological but must be transformative.

Rates per sector

Overall business rates revenue by key industry sectors prior to changes announced during 2016 Budget

(Sources: EY, VOA, HMRC, ONS, the Times)

12% Property, business administration and support activities

17% Manufacturing

9% Transport, storage, IT and communications

23% Retail

13% Finance, insurance, professional and scientific

Obstacles to investment

23% Complexity

26% Uncertainty

(Source: Chartered Management Institute, Gov.uk)

Apprenticeship levy

72% of parents support the planned levy

0.5% Levy as percentage of employer's total wage bill with a £15,000 upfront allowance

£3m Employers with annual pay bills in excess of £3m will pay levy from April 2017

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