

## Response to the Industrial Strategy Green Paper

This is the response of the Institute of Economic Development to the Industrial Strategy Green Paper. The Institute of Economic Development is the professional body of economic development professionals. We are a non-political body. This response has been composed after holding meetings, asking for member responses and seeking agreement from the Board.

The overall response has been pulled together by Nigel Wilcock, Executive Director and we would be delighted to clarify any points or make further more detailed comments / provide ideas as the Industrial Strategy is further developed. Our contact details are at the end of the paper.

We hope that the response is constructive and useful and we would be very pleased to discuss any or all of the points that we raise.

## Key Thoughts

- For consistency of delivery and a high priority being given to the Industrial strategy there is a crucial need to make economic development a statutory function within Local Authorities with a clear remit.
- Much of the Green Strategy contains ideas which have come and gone before – there is a need for a clear structure for delivery and then maintain this structure for the long term.
- Consistent Government priorities and spend in areas such as energy, transport, other infra-structure all help business invest for the long term – this is fundamental to allow business to invest and thrive and failures in this area in the past have undermined UK businesses in many of these industries.
- Far reaching change is needed to shift the imbalanced in the UK economy many of which are at least partially institutional. If scarce resources are to be used equally across the economy these imbalances must be addressed.

## Questions for consultation

1. Does this document identify the right areas of focus: extending our strengths; closing the gaps; and making the UK one of the most competitive places to start or grow a business?
2. Are the ten pillars suggested the right ones to tackle low productivity and unbalanced growth? If not, which areas are missing?
3. Are the right central government and local institutions in place to deliver an effective industrial strategy? If not, how should they be reformed? Are the types of measures to strengthen local institutions set out here and below the right ones?

Our response to these three questions is linked. Overall, we found that the Green Paper, whilst welcome, was somewhat limited in ideas for intervention. The scale of ambition was clear but the ideas on the means of achieving these ambitions were less far-reaching.

We agree that the ten pillars reflect those areas that need to be tackled and so the challenge now is to determine the more far-reaching activities that could be undertaken to deliver. There is also a belief that whilst these may be the correct ten pillars, some pillars are more important than others in delivering the balanced growth agenda.

Far-reaching ideas generally need a clear framework for delivery. One large concern of the Institute of Economic Development is that there is a complicated and ever changing set of organisations to deliver these ideas.

At the centre of this is how meaningful a central government green paper can be when many areas of England (and each of the devolved administrations) are involved in various stages of devolution. Some clarity on what Government's expectation is on how an Industrial Strategy should dovetail with the economic plans of those gaining devolved powers would seem essential. Without this a Strategy is the presentation of some ideas with the hope that some areas may pick up on some of the themes.

We also believe that some aspects of industrial strategy should be under the over-sight of Central Government – this is typically those aspects directly relating to sector development and where a piecemeal approach would be unhelpful or may undermine a nationally determined standard.

Central Government and a clear regional / local body are definitely the correct vehicles for delivering economic growth but the regional / local bodies have changed multiple times over many years and with the arrival of new bodies we do not always clear away the old leading to confusion, duplication and sometimes conflict. At present, in large LEP areas with no City and a two tier system of Government the Industrial Strategy offers limited relevance for District Councils.

It is our belief that Local Government should have a statutory responsibility for economic development and they are the local deliverers. Any different vehicles – combinations of Local Authorities, LEPs, and other sorts of development organisations are then the choice of Local Government according to their circumstances.

Without Local Government having a statutory responsibility, economic development will continue to be an amorphous soup which differs between locations, confusing those with whom it should be engaging and delivering less than it should.

A large aspect of what the Industrial Strategy should be concerned with is the relevance to the small business community which is the bedrock of the entire UK economy.

4. Are there important lessons we can learn from the industrial policies of other countries which are not reflected in these ten pillars?

Leading on from our comments above, there are undoubtedly things that we can learn on every incremental point and some of our experiences are set out in our response to the later questions, but overwhelmingly it is to create a structure (statutorily) and stick with it – this is the approach that has been taken in Ireland in the recent past, and there are many long-standing structures in economic development in neighbouring countries which have benefited from a clear remit and long term activity. Even in Scotland, we believe that the clarity between the work of Scottish Enterprise and the Local Authorities is a preferable model to that in place in England.

5. What should be the priority areas for science, research and innovation investment?

In many of the ideas concerning science, research and innovation, the Green Paper seems to presume that a continuum exists from university blue sky research, to new commercial ideas / applications through to product launch and success. This is a continuum which has not particularly driven significant economic growth elsewhere.

The experience of the US in this area, probably the location where fast growth innovative companies has been the most pronounced, is that companies or graduate / post graduate entrepreneurs take ideas and solve individual issues by working with universities / others.

High quality universities and their research is important in educating and expanding the horizons of graduates / post-graduates but the universities are not central to the innovation / application. The university expertise may be relevant again in solving the incremental issues in development.

University research can deal with long term research challenges, often set by Government, but it is typically companies that realise the applicability of research findings to industrial or market challenges. In many cases our universities are not structured to respond to application issues – although there are areas of good practice.

There also needs to be a clear strategy for how research is funded and collaboration enabled after Brexit is complete.

6. Which challenge areas should the Industrial Challenge Strategy Fund focus on to drive maximum economic impact?

As an economic development body, we are not qualified to speculate on the important technologies of the future – although our members have differing views.

An important question, given the comments made to question 5 would be whether the 'Industrial Challenge Strategy Fund' is the correct approach.

An interesting twist on this approach would be to invite UK based companies who carry out their R&D and value add in the UK to submit their R&D challenges for the next 5-10 years in conjunction with a University and to fund the ideas in that manner. The fund could then make stipulations about the location in which any innovation is commercialised.

At least such an approach contains an element of market thinking and avoids the suggestion that it is Government which is determining the winning sectors for the future. It also avoids picking sectors, carrying out research and then allowing the 'economic gain' to be developed offshore.

7. What else can the UK do to create an environment that supports the commercialisation of ideas?

The Industrial Strategy needs to recognise that different parts of the country have different economies and strengths. The strategy could encourage:

- Release of patents to enable innovation to be brought to market;
- Application of technologies that have been developed that are purposefully withheld for commercial reasons or are brought to market much more slowly which stunts the growth of innovation, for example battery and fuel cell technology.

8. How can we best support the next generation of research leaders and entrepreneurs?

The Industrial Strategy should focus on policies that would provide long-term investment to ensure strong national research infrastructure and a healthy UK research base across all disciplines, for example by investing in the development of skilled researchers, developing capability through fellowships and investing in doctoral training programmes and enhancing the flow of talent to all sectors.

Furthermore, the Industrial Strategy should support the interaction of R&D generated by institutions and entrepreneurs with commercial interests and the wider business community.

Overall there is a strong belief that business support is a priority and can be done more effectively than it is at present – in fact in many areas it has essentially been dismantled.

9. How can we best support research and innovation strengths in local areas?

Our members are strongly in favour of a proof of concept fund to test early stage ideas. Those with early proof of concept funding can then go on to try to develop further and raise commercial finance.

There are many US examples of 'fast track business growth' environments where developments are brought forward and there is a clear link to an access to funding combination at the end of the process.

The UK is seeing the development of new and interesting business centres / work hub environments but this is piecemeal with some local areas doing this better than others.

There is the potential for the sharing of best practice in the business centre / work hub approach but there is a need for these activities to provide the best advice to start-ups and have a clear link to finance, IP protection, growth advice etc. The link to these things is generally missing in the UK approach.

Germany established a national chain of incubators to try and create a more standardised approach. In the US, the Y Combinator programme is perhaps the best known of many. In the UK there is a long established network of Science Parks, with criteria established for what constitutes a Science Park but their presence and contribution is not referenced in the Green Paper.

10. What more can we do to improve basic skills? How can we make a success of the new transition year? Should we change the way that those resitting basic qualifications study, to focus more on basic skills excellence?

Our members have been keen to voice the interchangeable use of skills and qualifications – or a discussion about skills when we mean qualifications.

There is a continued discussion about whether *newly qualified* arrivals in the workplace are *sufficiently skilled* to add value to the employer. More work on placements and work-experience as part of the qualification process must surely be a good approach.

The section of skills in the Green Paper really needs to re-examine how mid-career members of the workforce are incentivised to continue their skills development. In a fast changing economy with an ageing workforce, the untapped potential of the existing workforce which may be under-employed or could be better deployed elsewhere will become very important. A tax credit system and greater availability of student loan funding for mature students undertaking a range of courses would be a starting point.

11. Do you agree with the different elements of the vision for the new technical education system set out here? Are there further lessons from other countries' systems?

12. How can we make the application process for further education colleges and apprenticeships clearer and simpler, drawing lessons from the higher education sector?

The new Institute of Technologies such as those proposed in Manchester, Birmingham, Doncaster and other urban areas will support skills gaps and routes in to technical education. However, there is a concern that IoTs will not have enough investment. One of the main challenges with an Institute of Technology is that the IoT is potentially yet another institution to an increasingly complicated delivery landscape. Learners need to be introduced to IoTs. There is further work to outline how IoTs can support learners and also how they benefit the education and training delivery market. Unless IoTs increase capacity their overall effect will be limited. Members believed that there are answers to these challenges (e.g. careers advice) but that how IoTs add value and contribute to technical education need to be communicated more widely.

Members thought that the idea of a technical / apprenticeship course finding process similar to UCAS was an excellent idea – whilst at the same time questioning whether enough funding had been allocated to this area to create a truly National network. Members do however think that there is a need for greater alignment of institutions with business needs. Main secondary education has little or no understanding of the businesses in the local economy with the result that high value added apprenticeships are not taken up and vacancies remain unfilled.

There was also recognition that more careers advice linked to skills selection is required. The careers advice in UK schools appears to be under-funded and diminishing in scale and quality.

13. What skills shortages do we have or expect to have, in particular sectors or local areas, and how can we link the skills needs of industry to skills provision by educational institutions in local areas?

It is the experience of members that engagement with local employers by the FE sector about their best understanding of skill requirements 5-10 years ahead is taking place in the areas where the FE College is best engaged with its employers.

One aspect of any statutory approach to economic development would be that every location has an active business engagement programme and this is certainly not the case in all areas.

The views of employers on skills, employment land requirements, future research opportunities, internal investment projects etc. should be systematically captured and acted upon – and this is not happening uniformly across the UK.

14. How can we enable and encourage people to retrain and upskill throughout their working lives, particularly in places where industries are changing or declining? Are there particular sectors where this could be appropriate?

Once an employee is in work, the loss of income / leisure time is a major barrier to future skills development. Where similar issues are encountered elsewhere in the economy, the use of tax credits is generally used as an incentive measure. This could be offered to employers to widen the skills of the employees (making their skills more flexible for the future demands of the workplace) and to employees allowing them to avoid some tax if they carry out valid personal development work with the view that they may generate higher taxes / avoid benefits in the future.

15. Are there further actions we could take to support private investment in infrastructure?

The East / West rail link between Oxford and Cambridge will represent a good example of how local stakeholders contribute to a scheme and this promises to offer a model that could be rolled out in the future. If this model proves successful then a framework that allows communities (local or regional) to come forward and show how some infrastructure developments could be part funded could be achieved.

This has not only been demonstrated at a national infrastructure level (Cross Rail, East West Rail, Manchester Metrolink) but also at a local level with things such as community broadband initiatives – with one small example being B4RN although there are no doubt many.

The M6 Toll also represents a project where private funding allowed access to new and improved infrastructure (compared to schemes which may start to impose a levy for infrastructure that the country has previously accessed for 'free') and there seems scope for more projects of this nature.

16. How can local infrastructure needs be incorporated within national UK infrastructure policy most effectively?

As above – through platforms that allow communities / stakeholders to demonstrate how their involvement can allow projects to happen more cost effectively when the infrastructure need is significant.

In general, a higher level of expenditure needs to be allocated to UK infrastructure – and infrastructure should not be confined to a discussion about transport for the workforce but also utility provision, digital connectivity and freight movement.

Digital investment in rural areas would seem to be a priority if economic growth is to be achieved evenly and the 'national assets' therefore be used more evenly.

17. What further actions can we take to improve the performance of infrastructure towards international benchmarks? How can government work with industry to ensure we have the skills and supply chain needed to deliver strategic infrastructure in the UK?

In the end, whilst innovative funding models can be put in place, the provision of infrastructure is about the consistent provision of funding to an international benchmark standard. The Netherlands is perhaps the best example of infrastructure provision in the world – and therefore a tremendous benchmark – but the amounts spent on infrastructure per capita are significantly in excess of the UK.

18. What are the most important causes of lower rates of fixed capital investment in the UK compared to other countries, and how can they be addressed?

Certainty of return linked to consistency of government policy is one important factor, capital allowances on expenditure are also a consideration.

Internationally fixed capital investment also tends to rise when labour costs increase. The UK has, in recent years subsidised labour costs for private companies through the provision of tax credits and this has, in turn kept unemployment lower than might have been expected.

Therefore, tax credits in the labour market are likely to have had an impact on fixed capital expenditure although the merits of this policy could easily be argued to be positive – and certainly the Institute is not advocating a dramatic change in policy in this area.

19. What are the most important factors which constrain quoted companies and fund managers from making longer term investment decisions, and how can we best address these factors?

This is a global issue related to stock markets, the nature of investors, and not considered relevant to a national industrial strategy – apart from stating that any industrial strategy needs to address the alternative ways in which businesses can raise equity in the UK without necessarily becoming public companies.

The medium sized manufacturing companies of Germany typically remain privately owned, supported in long term investment decisions by their banks and do not seek public equity finance.

The question is therefore how can we better fund our companies for long term investment projects? Not how do we fix the investment criteria of the public equity markets.

This is linked to the banking sector which is now risk averse, has huge due diligence costs which preclude relatively small scale lending, and the 'funding gap' between small scale lending and longer term / larger scale investment lending. There is a case for more public sector intervention in this area and the use of public sector investment (pension) funds.

20. Given public sector investment already accounts for a large share of equity deals in some regions, how can we best catalyse uptake of equity capital outside the South East?

21. How can we drive the adoption of new funding opportunities like crowdfunding across the country?

Quest 20 & 21. The question seems to assume that 'crowdfunding' investment and other un-regulated forms of investment are to be supported. This may be correct, but there are many other tax efficient intuitional forms of making contributions into investment vehicles than crowdfunding which have not yet reached saturation point and far more can be done to embed these in UK economic growth.

Opportunities such as EIS appear to be developed by Treasury but are then not integrated into the economic development frameworks of the UK but remain small scale tax incentives – this represents a lost opportunity.

22. What are the barriers faced by those businesses that have the potential to scale-up and achieve greater growth, and how can we address these barriers? Where are the outstanding examples of business networks for fast growing firms which we could learn from or spread?

Firstly, public policy is somewhat obsessed with fast growth, when actually if those individuals who have taken the step to create a business and employ people can remain in business then this is a boost to the UK economy. There is no current policy with any teeth that supports existing businesses with much of what existed now dismantled. Supporting business to survive will bring economic value – 'scale up' is achieved by about 6% of SMEs.

The wider comments about R&D, proof of concept, incubation, exporting, tax incentives, funding and banking / equity structures add to the support for those who wish to grow.

23. Are there further steps that the Government can take to support innovation through public procurement?

The reality of public procurement in major areas of expenditure is that contracts are let to multinational lead contractors and then the ability for UK SMEs to benefit from contracts is then often left to the decision making of the multi-national with little ability to influence the outcome of a contract for UK SMEs. There is the ability to make use of local content a key evaluation criteria in contract determination.

Annual Report accounting on SME involvement in supply chains would be welcomed.

Delays in payment are also a large deterrent to SMEs and the 30-day payment charter would be welcome here.

24. What further steps can be taken to use public procurement to drive the industrial strategy in areas where government is the main client, such as healthcare and defence? Do we have the right institutions and policies in place in these sectors to exploit government's purchasing power to drive economic growth?

There is much that can be done to drive industrial strategy through procurement.

Perhaps the most important step is to provide certainty of demand. Over decades the UK has changed its policy in areas such as energy, transport and defence – or where policy has remained the same the demand has been ‘lumpy’ moving from one area of expenditure to another rather than spending a relatively steady level over time.

This lack of certainty has either deterred investment or caused the failure of those businesses which were in the UK but for whom demand was insufficient – only for the demand to return again at a later date and leave the UK reliant on imports / foreign capital (rail, bus, nuclear etc.).

25. What can the Government do to improve our support for firms wanting to start exporting? What can the Government do to improve support for firms in increasing their exports?

Micro and small businesses will have a limited impact on the UK’s export performance, take a large amount of support to get close to exporting and the opportunity cost for that business of exploring exporting is potentially damaging to their UK performance.

Medium sized business and large businesses are the key to making a larger impact on the UK’s export performance.

At present the DIT network internationally is seeking to focus to a greater extent on medium and large businesses but the outsourced ITA network across the UK is incentivised to find large numbers of companies who are interested in exporting and these are generally small / first time exporters. The export support network in the UK is therefore currently mis-connected.

This is an easily corrected technical / practical point.

A further issue is that a large number of high performing medium sized UK businesses have been acquired over many years by foreign capital. This is not an economic issue in itself until the question of exporting is considered. A foreign owned business is generally likely to direct export effort from Head Office with the UK subsidiary left as an outpost.

One consideration could be tax incentives on export based turnover to incentivise UK subsidiaries to undertake their export from their UK base.

26. What can we learn from other countries to improve our support for inward investment and how we measure its success? Should we put more emphasis on measuring the impact of Foreign Direct Investment (FDI) on growth?

The UK previously offered ‘always available’ financial incentives for inward investment under the Regional Aid Block Exemption. The approach was amended with the introduction of the Regional Growth Fund – but as a scheme that only opened at set times for applications this did not suit inward investors, and it has subsequently disappeared.

The reality of this grant scheme was that it allowed Government to maintain a dialogue with a number of investors even when they invested in the UK but did not follow through a grant application. In addition, any awards which were made, were soon paid back in various tax measures.

This is seen as an apparently highly attractive offer for business – but actually in reality a low cost solution for Government. In addition, by not offering such an approach the UK is now disadvantaged against many other locations (it should be noted that the devolved administrations maintained such a scheme).

It is our view that more emphasis should be put on FDI for capital investment – large sunk capital costs are made for long term economic activity and the UK has always favoured the measurement of employment over capital creation. In addition, investments that are at the top of a supply chain should also be seen as the highest priority because of their ability to drive further activity beneath them.

27. What are the most important steps the Government should take to limit energy costs over the long-term?

28. How can we move towards a position in which energy is supplied by competitive markets without the requirement for on-going subsidy?

Questions 27 & 28 can be considered together. There is an opportunity to create local distributed networks in strongly manufacturing locations rather than businesses having to rely on the national grid / provision of electrical capacity by the infrastructure providers. The infrastructure requirements / connectors for this are often the barrier to implementation and this could be the area for intervention to create competitive 'high intensity energy parks'.

This has been achieved in some locations through waste from energy and heat networks.

29. How can the Government, business and researchers work together to develop the competitive opportunities from innovation in energy and our existing industrial strengths?

One area of massive opportunity would be to consider buildings and their use focusing on understanding energy within design, construction, renovation and use.

30. How can the Government support businesses in realising cost savings through greater resource and energy efficiency?

Questions 29 & 30 can be considered together. The current European State Aid Block Exemption allows the use of state funds to be used to better incentivise those projects which are some distance from using standard technology. This is an area of state aid funding in which the UK has undertaken little work but could incentivise the largest users and this could bring forward demonstrator technologies.

31. How can the Government and industry help sectors come together to identify the opportunities for a 'sector deal' to address – especially where industries are fragmented or not well defined?

32. How can the Government ensure that 'sector deals' promote competition and incorporate the interests of new entrants?

Answer to 31 & 32

This was seen as an innovative area of the Industrial Strategy and partly because it was led by the private sector leaders themselves. We would argue that this is an area which should be left with the sector leads and the question of definition, making a difference and appropriate government intervention be left as an idea for them to debate.

The expectation is that the sector leads will come up with ideas linked to the remainder of the Industrial Strategy which is great – and if they bring new ideas then this would be useful as well.

Where industries are 'not well defined' there is a suggestion from the question that Government knows the definition that people should be working to and that the market has somehow got it wrong. In fact, where companies don't really fit into the Government definition of the sector but are combining well to serve a market need, the suspicion would have to be that Government hasn't got the umbrella sector term correctly defined – examples of 'advanced manufacturing', 'creative industries' and 'environmental technologies' might be considered those areas where the terminology of Government is so broad that its meaning is lost in translation to business.

Sector deals therefore need to focus on real sectors and be delivered to the sector agenda.

When sectors are correctly defined and areas of need and future innovation are identified it will be in the sector's best interest to draw in new entrants / encourage current players to innovate. The role of Innovate UK working with the Sector Deals will be important in this area.

We are also concerned that in the entire Industrial Strategy no mention is made of Catapults (of for that matter Science Parks). Catapults were supposed to be the answer to sectors and innovation and were modelled on German Fraunhofer Centres – it is surely too early to ignore these – and this is another example where we have to stick with structures longer

term and if they aren't working then remodel them – but don't just let them limp on broadly ignored once the next policy comes along.

33. How can the Government and industry collaborate to enable growth in new sectors of the future that emerge around new technologies and new business models?

If the innovative strategy expressed in our answers to (5) is brought forward, the UK's approach to research and innovation will be more attuned with business rather than focused on the blue sky research of Universities and this will go much of the way to addressing this question.

34. Do you agree the principles set out above are the right ones? If not what is missing?

We completely agree that research and development which is closer to the market, draws in those with the scientific background that can solve incremental problems, funds proof of concept, provides space for collaboration, provides R&D credits that can be spent on UK establishments, Government funding that restricts some activities to the UK and a closer link between support agencies and private commercialised funding could be likely to create strong benefits to the economy.

35. What are the most important new approaches to raising skill levels in areas where they are lower? Where could investments in connectivity or innovation do most to help encourage growth across the country?

Clearly raising skill levels is a laudable aim and an activity that may benefit from innovation that is outside the remit of the IED.

A slightly recurring point in our responses to these questions and one which is at the centre of our summary is whether this is the correct question. One reason why some regional locations have a lower proportion of higher level skills is that the population that achieves higher levels of attainment then leaves the area.

Skills shortages may partly be because of a lack of aspiration but they are also linked to a lack of high achieving student / graduate retention or graduate returners.

The answer to the question becomes a more balanced geographic spread of opportunity would lead to a more balanced distribution of skills.

The answer to the connectivity question is then – there are some well performing areas which will perform well because of critical mass and economies of agglomeration. These are the areas that are a lower priority for connectivity because they are successful. There are other areas of opportunity but for reasons of scale and the tyranny of distance, are under-performing. There is an argument that these locations need to have best connectivity – and in today's world this is likely to mean digital connectivity. The suggestion is therefore that rural broadband becomes a very clear priority.

36. Recognising the need for local initiative and leadership, how should we best work with local areas to create and strengthen key local institutions?

37. What are the most important institutions which we need to upgrade or support to back growth in particular areas?

38. Are there institutions missing in certain areas which we could help create or strengthen to support local growth?

Ques 36-38. Clearly institutions can help – but the answer is that any 'tier one' institution in a region can make a significant difference because they change the economic and market habits of suppliers and customers in the way that a 'branch office' of an institution does not.

In the UK typically Government, regulatory, procurement, legal and financial decisions are taken in London. As a capital city transport links have gravitated towards London. The focus of decisions being taken in London leads to businesses visiting

London and then invariably creating a base in London which may then become head office. The scale of opportunity becomes a magnet for talent. The cycle continues.

The main problem with this gravitational pull approach is that the country has invested in assets outside the capital which are under-used whilst the capital is under strain and there remain commercial opportunities elsewhere which are commercially under-exploited.

The answer therefore is not which institutions (and therefore perhaps by inference which additional branches of the UK supportive infrastructure) should be in regions – but rather which bits of centralised UK institutional activity can be completely decentralised / or centralised in a location other than London.

The entire UK political and economic system is institutionally biased in favour of London and this is important because it under utilises the full economic potential of the UK.

**In addition:**

As the Green Paper turns towards a delivery approach we would expect to see a clearer action plan, timescales and measurements of success. Much economic strategy in the recent past has lacked a clarity concerning delivery. Our members stand ready to assist in the refinement of the Green Paper and the delivery of the plan.

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