Industrial Strategy

for a more prosperous, fairer Britain

Industrial Communities **Alliance**

- **Provide an economic context in which industry can prosper**
- **Hold the line here: Britain should not abandon any more sectors of manufacturing production**
- **Welcome free trade – but only on the basis of fair competition**
- **Use public procurement as a tool to support British industry**
- **Make sure the banks provide long-term finance to industry**
- **Exploit the scope to provide aid to industry**
- **Target resources at the high-level technical skills that industry needs**
- **Invest more in the infrastructure schemes that really matter to industry**
- **Support energy-intensive industries by reducing their bills**
- **Harness Britain's innovative strengths through effective research and development**

Britain's economic problem

The British economy is fundamentally imbalanced *– and the country's prosperity is deeply precarious as a result.*

In the wake of the financial crisis in 2008 and the subsequent recession, many commentators talked about the need to rebalance the economy away from financial services towards production, investment and exports. The Chancellor called for "the march of the makers".

This hasn't happened. The British economy remains at least as imbalanced now, if not more so, than before the financial crisis. Manufacturing output, for example, has still not recovered to its pre-recession level. The consequence is that the UK economy continues to display a number of alarming features:

- *An extraordinary level of* ***household debt*** *– among the very highest in the world*
- *A public sector* ***budget deficit*** *that remains large despite the most draconian austerity measures in modern times*
- *A* ***trade deficit*** *with the rest of the world, in goods and services, at all-time record levels*

These features of the contemporary UK economy are actually deeply interrelated. In essence, the UK is living beyond its means. Consumption and living standards are being sustained not by incomes earned by trading with each other and the rest of the world but by ever-rising debt and the sale of UK assets – companies, property, government bonds – to foreign investors.

If investors lose patience or faith in the UK the consequences are dire: a collapse in sterling, higher prices, higher interest rates, lower living standards, falling house prices, recession and still more public debt and even more austerity.

The reason why the UK finds itself in this precarious position is that it has neglected its industrial base.

It used to be said that Britain was 'the workshop of the world' but that was many years ago. In the 21st century Britain's claim to fame is more likely to be as financial capital of the world – or at least as one of its financial capitals – and maybe as a cultural capital too.

That Britain has proved so good at selling services to the rest of the world – finance, legal, design, media, education and the rest – is immensely welcome. There is also, no doubt, more that could still be done to promote the export of British services around the world. But the successes of the service sector should not obscure the failures in manufacturing. Nor should we be lulled into thinking that the successes of one offset the failures of the other.

- *Around **half the value of all UK exports** still comes from manufacturing*

- *Manufacturing, with just **10 per cent of the UK workforce**, therefore sells as much to the rest of the world as the other 90 per cent put together*

- *But it is **trade in goods**, not services, in which the UK deficit is so staggeringly large*

- *And after years of neglect, British manufacturing is effectively **'hollowed out'** – whole sectors have simply disappeared.*

It is wrong to think of 'industry' as something from the past. This may be the reality in too many former industrial towns but industry remains central to every other major advanced economy.

It is also wrong to think that high-wage economies like the UK cannot retain a large manufacturing sector in the face of competition from China and other developing countries. The experience of Germany, where labour costs are generally even higher than in the UK, robustly refutes this claim. In Germany, the share of manufacturing in GDP is more than double the level in the UK – and Germany has a huge trade surplus.

*Unless the alarming long-term trends in industrial production are addressed the British economy faces a bleak future. At a time when **productivity growth** in the UK is flagging, industry can provide high-value added jobs. Industry can also provide the **exports** to begin to bring the economy back into balance.*

*This booklet sets out an **industrial strategy for Britain**.*

The strategy has been developed by the Industrial Communities Alliance, the all-party association of local authorities in the industrial areas of England, Scotland and Wales. The strategy isn't the result of a one-off study by a consultant or think tank. Rather, it distils the accumulated knowledge, experience and views of local authority members and officers across the country. On industrial matters, that body of expertise is often formidable.

Alliance areas are the places that have suffered most from failures to nurture Britain's industrial base. Whole sectors – coal, steel, textiles, shipbuilding, heavy engineering – have disappeared entirely or been reduced to a shadow of their former selves. The communities left behind now often have to get by on low-paid work in call centres or warehousing – or on benefits as a main or top-up source of income.

*A revival in British industry would be especially beneficial to the economies of the **Midlands, North, Scotland and Wales**. Within these regions, it is also the places beyond the big cities that would often benefit most. This is where much of what is left of British manufacturing can still be found, and where economic problems are often greatest.*

*An effective industrial strategy can enhance **competitiveness** and help deliver a **high-wage, high-employment economy**.*

A rebalancing of the economy towards industry is a win-win strategy:

- *What the UK economy needs to **sustain prosperity** is a shift towards production, industry and exports*

- *What a shift towards industry would also deliver is a **fairer Britain**, with less reliance on London (with all its attendant problems of congestion and high costs) and the potential for a sustainable revival in many of the hardest-pressed cities, towns and communities up and down the country*

Economy

Provide an economic context in which industry can prosper

Industry needs the right economic context in which to flourish. It is easier to promote investment, growth and jobs when the management of the economy reflects companies' needs. At a minimum that means:

- **A low exchange rate** that enables British businesses to compete effectively on domestic and international markets

- **Low interest rates**, to make borrowing cheap and help foster investment in plant and machinery

- **A measured approach to deficit reduction** that recognises the need to sustain the overall level of spending in the economy

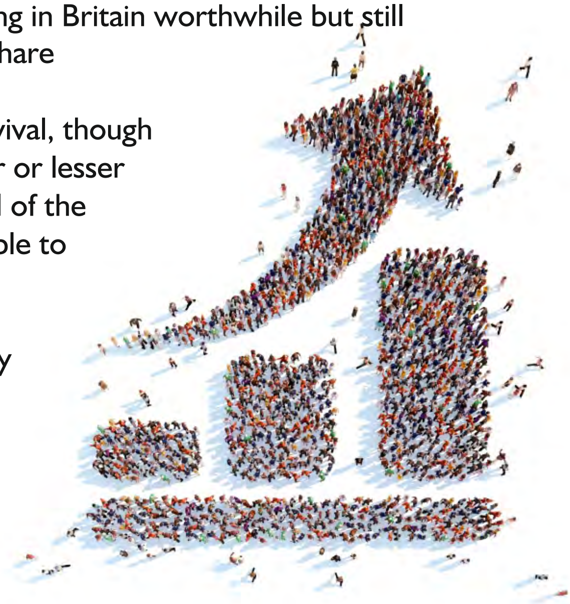
On the supply side of the economy there also needs to be:

- **Regulatory regimes** that ensure the protection of workers, consumers and the environment but do not hinder investment and growth

- **Business taxation** that makes investing in Britain worthwhile but still ensures that companies pay their fair share

These are all prerequisites for an industrial revival, though they have rarely all been in place. To a greater or lesser extent, they are all variables under the control of the Treasury and the Bank of England, or susceptible to their influence.

But these prerequisites need to be matched by other practical actions.



Manufacturing

Hold the line here: Britain should not abandon any more sectors of manufacturing production

Over the last fifty years, under the tenure of successive governments, the list of industrial sectors from which Britain has withdrawn has become far too long.

This is rarely because there is no demand any more for these goods. Britain is still a trading nation but no longer builds merchant ships, for example, and even the burgeoning demand for cruise liners is met by yards in France, Italy, Germany and Finland. We still use coal, but the last British colliery closed in December 2015.

The **steel industry** is the latest example of a major British industry whose very existence is under threat.

There has been much talk of 'backing winners' at the higher-technology end of production – in pharmaceuticals, graphene and nanotechnology for example. Support for these sectors is welcome but they are too small in the current economy, whatever their long-term future, to offer the only way forward.

Quite simply, it is time for government to say enough is enough: we hold the line here. The UK economy needs a large manufacturing sector to deliver sustainable prosperity so it is vital to hold on to what we've still got. That doesn't mean keeping every factory but it does mean that the capability to produce in any major sector should not be lost and that **anchor companies** – the drivers of local and national supply chains – should be nurtured.

The **reshoring** of production from abroad should also be encouraged.

How to deliver these aspirations would need to be worked out on a case-by-case basis. What is needed to save the steel industry, for example, will not automatically apply to other sectors. What is important is the **overarching policy commitment**: the destruction of manufacturing industry should be allowed to go no further.

Trade

Welcome free trade – but only on the basis of fair competition

Free trade has brought the benefit of cheaper goods and services, to Britain and to the rest of the world economy. The effects of competition are broadly positive, even if at times painful.

Access to the **European single market** is important for many companies – in the car industry for example – and this must remain a priority as the UK leaves the European Union.

However, there need to be **firm limits to free trade**. Competition may be welcome but it must be fair.

The dangers of present free trade arrangements, and the shortcomings of protection measures, have been highlighted by the steel crisis. China has a vast surplus of steel production which it has been dumping on the world market at **subsidised prices**. The UK steel industry has been directly in the firing-line, at home and in its export markets.

Worryingly, steel could be only the first market to feel the effects and the market distortions of the slowdown in the Chinese economy.

More generally, British manufacturing should not be allowed to suffer as a result of unfair competition from countries that fail to respect **workers' rights, health and safety or environmental obligations**. In trade with the EU, at least, this should not happen. In trade with some other countries, questions need to be asked.

The UK government should back free trade – but not at any price.

Procurement

Use public procurement as a tool to support British industry

Public sector procurement has the potential to play an important role in fostering British industry. Plenty of UK firms have the capacity to supply UK needs. Sometimes potential suppliers are right on the doorstep. But too often the contracts seem to go elsewhere for little obvious reason.

Orders should not necessarily be earmarked for specific firms but it is still possible to introduce a range of socio-economic requirements into contracts, for example to:

- Draw on local **supply chains**
- Provide **apprenticeships** for local workers
- Recruit from among the **long-term unemployed**
- Earmark a proportion of sub-contract business for **small firms**

In addition, through collaboration and dialogue it is possible to ensure that the timing, scale and specification of big public sector contracts allow UK suppliers to be prime candidates. In this regard the UK would be going no further than existing practice in much of the rest of Europe.

The Westminster government now encourages **pre-procurement discussion** with potential suppliers but this requires a cultural shift that needs to become embedded across the whole of the public sector. 'Lowest cost' matters, but not to the exclusion of all other considerations.

Local authorities are mostly only too willing to play their part in supporting local businesses so long as they can be confident their actions are legal and above board.

Finance

Make sure the banks provide long-term finance to British industry

The relationship between British banks and British industry is the enduring tragedy of the British economy.

Manufacturing firms need long-term financial support at reasonable rates of interest. The banks, however, prefer to invest for short-term financial gain. Money that should be used to finance investment in plant, machinery and working capital is instead used to finance ever more household borrowing and speculation on world markets.

Germany demonstrates only too clearly that it doesn't have to be like this. German banks are renowned for their long-term financial collaboration with manufacturing companies and this has been a key factor behind the success of world-leading German brands.

British banks need to be challenged over their investment behaviour. They are sure to complain loudly but the time has come to face them down.

The UK government and the Bank of England have levers they could deploy to shift banks' behaviour. The **Funding for Lending** scheme introduced in 2012, which played a key role in kick-starting the economy, made cheap finance available to the banks but with the requirement that they increased the volume of their lending. The banks snapped up the cash, though rather predictably used nearly all of it to increase mortgage lending. The point is that the banks can be incentivised to change their behaviour – and it is investment in industry that needs to be the target next time.

The government-owned **British Business Bank** offers help to small firms but the big banks should not be let off the hook, especially in their dealings with larger companies.

Business support

Exploit the scope to provide aid to industry

A key tool in rebuilding Britain's industrial base is the ability to offer companies public sector financial support to deliver investments that otherwise wouldn't have gone ahead, or perhaps not gone ahead on the same scale, on the same timetable or in the same place.

EU competition rules generally frown on this type of support but whether they will remain a condition of UK access to the single market is unclear. In any case, the rules still allow financial support towards the cost of:

- Training
- Research and development
- Environmental compliance
- Investment in less prosperous local economies

The last of these – **regional aid** – is especially importantly in the context of older industrial Britain. The aid intensity that is allowed in the 'Assisted Areas' is higher than elsewhere and greater for SMEs than multinationals.

The UK doesn't have a good track record of exploiting the scope within the rules to deliver support to British industry

In **England** under the Coalition Government, the Regional Growth Fund was the main tool for supporting industry in less prosperous areas, carrying on from where previous schemes dating back to the 1960s left off. But **the funding has now run out**, with no planned successor.

The **Scottish and Welsh Governments** remain committed to business support – and in the poorest parts of Wales the leeway under the EU rules is considerable – but there is only so much that the devolved administrations can achieve with their relatively limited budgets.

Skills

Target resources at the high-level technical skills that industry needs

Some employers flag up **skill shortages** when in practice they really don't like to pay the wages to attract the workers they need. But in the context of UK manufacturing there is more than a grain of truth in claims of a skills shortfall.

In the 1980s and 90s, when manufacturing employment plummeted, the old apprenticeship system essentially broke down. It wasn't perfect, but what it has been replaced by is a hotchpotch of short-duration schemes and college courses that hasn't really plugged the gap. Too many of Britain's most skilled workers are now getting too old.

Once again, this stands in stark contrast to Germany, where an internationally admired system combines high-level formal education with on-the-job training in industry. On skills, **Britain needs to become more like Germany**.

In practice this will not be achieved without government intervention – employers can't just do this for themselves because the unscrupulous will always duck their responsibilities and poach those trained elsewhere.

The **training levy** on large employers, introduced in April 2017, is a step in the right direction. It should fund skills development that:

- Works with manufacturing employers
- Prioritises industrial and technical training
- Complements existing provision by the devolved administrations and other local players
- Is sensitive to the difficult financial circumstances confronting local authorities

Infrastructure

Invest more in the schemes that really matter to industry

Britain risks going down a blind-alley in prioritising a handful of expensive prestige projects rather than the more numerous, more incremental investments that industry needs.

Speeding business travellers between city centres, for example, does not necessarily make much difference to a chemical producer on Teesside, a steelmaker in South Wales, a shipyard in Cumbria or a car maker on Merseyside.

What industry really needs is:

- The renewal of Britain's **energy infrastructure**, including the construction of new power stations, to guarantee affordable and reliable electricity supplies

- A plentiful supply of **sites and premises**, underpinned where necessary by flexible planning and gap funding for development on brownfield sites and in priority areas

- Investment to **ease bottlenecks** in the road network to speed the flow of goods and provide reliability, including to ports and airports

- Investment in **rail freight** capacity

- **Super-fast broadband**, including in smaller towns and rural areas

- **Flood protection** in vulnerable areas

Investment in infrastructure also provides a key source of orders for industries such as steel and engineering.

The Treasury needs to move away from appraisal techniques that prioritise saving travel time towards a wider perspective that includes the economic development benefits of infrastructure investment.

Energy costs

Support energy-intensive industries by reducing their bills

Some manufacturing industries are unavoidably energy-intensive – steel, ceramics, aluminium, cement and heavy chemicals for example. The energy input can't be reduced much if at all, otherwise producers would have done so years ago.

Government figures show that energy-intensive industries employ around 600,000 people and contribute £52bn a year to the UK economy.

Carbon taxes are a useful tool to incentivise the move towards a greener economy but their applicability to energy-intensive industries doesn't make sense.

There is no point if the effect is merely to shut down UK plants and transfer production to other countries where environmental regulations are less stringent. This process – sometimes called **carbon leakage** – simply leads to the same quantities of pollution elsewhere, or possibly even more. The UK might feel virtuous about not being the guilty party, but UK jobs would be lost for no net gain to the global environment.

The UK government has been slow to wake up to this reality and the delays have been a factor compounding the crisis in the steel industry.

Limited **financial compensation** for energy intensive industries was first announced in the *2011 Autumn Statement* but it took until 2016 to bring some of the measures into force. The *2015 Autumn Statement* announced further exemptions from green energy charges – but not until April 2017.

Policy is heading in the right direction but energy intensive industries need a clear signal that their **international competitiveness** will not be undermined by green energy charges and environmental regulation.

R & D

Harness Britain's innovative strengths through effective research and development

Britain is actually very good at primary research. Its universities include some of the best teams in the world and there is no shortage of scientific experts at the very highest levels.

Where Britain too often falls down is on **transferring knowledge** and innovation from the laboratory to the shop-floor in industry.

The problem is not new, but the challenge is to bridge the gap. Valuable starting points would be to:

- Shift formal **management education** away from its narrow 'business school' focus on financial variables towards a better understanding of the role of science and technology

- Build **academic/industry partnerships**, not just at the local level where they help small firms but across the country as a whole to engage larger companies

- Extend the number and reach of the government-funded **Catapult Centres** that currently promote networking and innovation in ten high-technology sectors

- Build on the **advanced manufacturing park** concept, bringing together research and production on the same site

- Deploy the public sector **financial support** for companies' R&D that is allowed under competition rules

The Industrial Communities Alliance is the all-party association representing some 60 local authorities in the industrial areas of England, Scotland and Wales.

The Alliance was formed in 2007 by the merger of the longer-standing associations covering coal and steel areas and also includes a wide range of other industrial areas.

The aim of the Alliance is to promote the economic, social and environmental renewal of the areas covered by its member authorities. The Alliance works with the governments and parliaments in London, Edinburgh and Cardiff, with development agencies and with its own member authorities.

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