

in pursuit of
GROWTH

The Rt Hon the Lord Heseltine of Thenford CH

**‘Unless I can secure for the nation results similar to those which have followed the adoption of my policy in Birmingham ... it will have been a sorry exchange to give up the town council for the cabinet.’
(Joseph Chamberlain).**

NO STONE UNTURNED

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October 2012**

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One man's vision

- > our shared responsibility for creating wealth

The worst economic crisis of modern times

- > the scale of the international challenge

Localism – building on our strengths

- > reversing a century of centralisation
- > enhancing the standing of Local Enterprise Partnerships (LEPs) to bring together partners across the private and public sectors to drive local growth
- > empowering LEPs to lead local economic development through a major devolution of funding

Whitehall – a confident, strategic centre of government

- > delivering the Prime Minister's vision for growth
- > a smaller and more highly skilled central government machine
- > a strategic partnership with all sectors of the economy

Government and growth – catalyst, enabler, partner

- > decisive government leadership for major infrastructure projects
- > effective public sector procurement, driving innovation and securing our industrial base
- > maximising the benefit of the UK's research base

Private sector – broadening the capacity for excellence

- > raising the ambition and capabilities of the average business
- > a new role for chambers of commerce
- > a voice for UK plc

Education and skills – the foundation for growth and prosperity

- > the end of underperformance
- > a role for employers in the education of the children they will one day employ
- > ensuring investment in skills reflects the jobs available

Making it happen

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One man's vision

The Government should set out a comprehensive strategy for national wealth creation, defining its view of its own role – and the limits of that role – together with those of others in local authorities, public bodies and the private sector.

This report makes 89 recommendations.

Some will say they are criticisms.

That is exactly the wrong approach.

To invite criticism is a sign of strength.

To accept it is a sign of confidence.

We are all too close to the economic crisis.

There is opportunity on a grand scale.

Huge infrastructure demands and hungry institutional funds – link them.

Excellence in industry, commerce, academia – extend it.

England's cities pulsing with energy – unleash it.

Every one of us needs to rise to the challenge.

1. In March 2012 the Prime Minister asked me to report to the Chancellor of the Exchequer and the Secretary of State for Business as to how we might more effectively create wealth in the UK.
2. The Chancellor announced the terms of my review on 21 March and offered me the support of a cross departmental team of officials to assist in the task. I cannot overstate my gratitude for such a privilege or for the dedication with which that team has worked to reflect my views even where they conflict with departmental policies. The views expressed here are entirely my own although they have been much influenced by the large number of people from all aspects of our society to whom we have spoken and to whom I am indebted.
3. We are experiencing the worst economic crisis of modern times. As a consequence many of the old certainties have come under intense scrutiny. There is a hunger for ideas that could contribute to the restoration of growth. There is no shortage of proposals. But what strikes me – and encourages me – is the unanimity of, among others, the CBI, TUC and The Times that Britain needs an industrial strategy. The very words are controversial. With them comes the baggage of past attempts and past failures.

My history – business and government

4. It is 57 years since I moved to London from Oxford University and my home in Swansea. Two formative experiences since then have profoundly influenced my views. These are central to the report I write today.
5. First the experience of leaving a small business to become a minister of the Crown in 1970. My journey in business started as half owner of a boarding house in London. From there we moved into property development, the construction industry, employment agencies and publishing. We made mistakes, bad judgements and were over confident. Fortunately the good judgements outweighed the bad. Cash was always tight but by the time I left to join the Government we employed 400 people.
6. My early speeches would reveal my support for the simplest of notions of the role of government. Get off our backs, cut the red tape, deregulate, lower taxes. My laughter would have been loudest at Ronald Reagan's later joke – 'I've come from the Government. I'm here to help'.
7. Before leaving the company I was still involved in the minutiae of everything that happened in the business – even approving every petty cash voucher over 50p. By contrast, on my first day in government I was asked to read a few pages and sign off the £6 million electrification of a rail line in the east of England. I asked to see the managers responsible. 'Minister, if you start doing that you will be left with no time for your official work'. It was clear from the start that government ministers were meant to approve papers and make decisions, not involve themselves in the hard grind of turning those policies into reality. This was the public sector, although on that occasion I did see the managers.

- 8.** My subsequent journey in government was broad: the complexities of local government reform, the planning system, Britain's role in space, the saving of Rolls-Royce, Concorde, defence procurement, our international competitiveness agenda. Time and again I was confronted by the way other governments aided and supported their wealth creating capabilities. My view of government's role was never quite so simple again.
- 9.** Experience indicated that there are some things only government can do to drive growth in the economy. It must do those relentlessly and to the very highest standards set around the world. There are many areas where government should stand aside completely. But in the vast majority of cases we will only get the very best results for our economy if government, the business community and local leaders exploit their skills and resources in partnership.
- 10.** Whether we look at the well established mature economies such as the United States or the new thrusters of the BRICS – Brazil, Russia, India, China and South Africa – there is one clear message we overlook at our peril: the public and private sectors are interdependent. Only by working together and learning to understand each others' strengths and capabilities will we succeed.
- 11.** The second formative experience was Liverpool and the 18 months I spent visiting the city and its surrounding area after the riots of 1981. This immersed me in the realities of one of England's greatest cities. The Prime Minister accepted the argument that the riots were not just the reaction of a gang of yobs on the street. They were the result of deep, intractable, social and economic issues which the Government had a duty to address. It was important to get under the skin of the issues.
- 12.** People often ask me if my experiences in Liverpool changed my views and are surprised when I say no. I had long believed in the individual as central to the process of innovation and enterprise, and was firmly committed to the value of choice and competition as integral to decision making in both public and private sectors. I believed enterprise was a natural human condition, invaluable in driving excellence and growth. More than a decade of front line political experience had taught me as well of the vital role of government and the public sector in securing essential public services and facilitating the growth of the economy.
- 13.** What Liverpool forced me to confront was the extent to which these conditioning qualities had been driven from municipal England. The dynamism that had built the city was gone. Leadership relied on London. Liverpool's challenges could only be overcome if the local community was engaged and enthused to harness its resources and build on its strengths in a much more effective partnership with central government.
- 14.** Over many decades, power and initiative have shifted under governments of all persuasions from provincial England to its capital city and its bureaucracies. Strong local leadership in our great cities created the industrial revolution and made us what we are. London did not dominate. But of course the social conditions of those living in the

industrial cities were quite unacceptable. A long democratic process rightly tackled the consequences of urban squalor and often acute poverty. But in the process local initiative gradually moved from the enterprising industrialists to the councillors of today – much more preoccupied with a social agenda than earning the wealth to pay for it. And as the costs of such social provision relied increasingly on central government, so a range of circulars, ring-fenced grants, hypothecated funding and a new breed of quangos further eroded local discretion. Local government assumed the character of Whitehall's branch offices. The private sector has a remarkably similar profile. To an extraordinary degree head offices are London based, or overseas. Regional managers have replaced the enterprising leaders.

- 15.** In government, careers focus on functions. Initiatives concentrate on specifics. There are still few, if any, dialogues in Whitehall that start with the strengths and weaknesses of place or community. In this we are unlike any of our equivalent economies that build on local diverse strengths. We have created in London a functional monopoly.
- 16.** Big government does not work. Ministers and their officials are not that clever. Events are not that predictable. Yet no government can stand apart, indifferent to the results they achieve from the resources they spend on taxpayers' behalf. The challenge is to create a more balanced partnership – embracing the strengths of our cities and regions, and the resources of government.
- 17.** Government must now reverse the trend of the past century and unleash the dynamic potential of our local economies. The Government is committed to a local agenda. Is that policy or slogan? There are encouraging signs to believe it is policy but so far we have seen only the first steps.
- 18.** In the private sector, British success stories are numerous. We have world leading businesses, delivering innovative products and services to markets at home and overseas. But our overall attainment is judged by the performance of the average business. And the average business in the UK is simply not strong enough.
- 19.** Successive administrations concerned to boost productivity have had a tendency to concentrate on the issues faced by SMEs. No one has greater admiration for the vibrancy and ingenuity of the men and women who run these businesses than me. But we cannot be blinded by such a simplified approach. A complex economy has something of the nature of a rainforest. Take away the canopy and the sun will destroy the myriad species beneath. So it is that our major corporations sustain the thousands of small and medium size businesses in their supply chains. Without equal focus on the needs and competitiveness of our large and mid-sized businesses, the Government does a disservice to the very SMEs it wishes to support.

- 20.** A serious opportunity to improve the ambition and capability of British businesses has long been ignored by the failure of successive governments to act on Lord Devlin's report of 1972. His objective was to help the private sector create world class support systems and thereby raise their game. He focused in particular on the role of chambers of commerce and trade associations.
- 21.** Devlin's proposals remain largely ignored. If localism is to mean anything, if the private sector is to lead a renewed search for growth and a major increase in exports across the world, we need British businesses to have support systems comparable with those of our competitor economies.
- 22.** This failure to act on Devlin's proposals can be seen in a wider context. It is well over a century since concerns were aired that our education system was failing to improve in line with Germany and the US. Again many of the issues in this report are not new. In 1985, a House of Lords Select Committee¹ made recommendations when looking at the implications of the deficit in the UK's balance of trade in manufacturing. Its report pointed to the need for: an improvement in industrial competitiveness; a coordinated industrial policy, led by a Cabinet committee; government support for innovation and exports; promotion of business investment; an education system that is more responsive to the needs of industry; and better management training in business.

So what now?

- 23.** As we look to the economic challenges our country faces today, we should ask ourselves whether we are doing a good enough job. That question applies to us all and is not answered by pointing to the many examples of excellence in our country. Even when the economy picks up again, will our economic performance be as good as it could be? The long term evidence would say it will not. Are there lessons we can learn from how other countries divide responsibilities between government and the private sector, or between the centre and our cities and regions? There are.
- 24.** There is a temptation to select a handful of popular explanations for Britain's economic decline. That is not to say that tax, regulation and bureaucracy are not important. They are, but they are part of a much broader picture. I have tried to make this report as thorough and comprehensive as possible, although it is important to recognise that to do so in six months imposes its own constraints.
- 25.** This report sets out the case for a major reconfiguration of responsibilities for economic development between central and local government, and between government and the private sector. Throughout discussions for this report, and based on the experience of the last 40 years in and around government, I have heard time and again that the Government needs a single compelling vision for how wealth will be created in the UK. It is said that all parts of government, not just the Business Department or the Treasury, must work in

¹ Report from the House of Lords Select Committee on Overseas Trade, 30 July 1985

support of that plan. Decisions on housing or transport, education or welfare support will have a far greater long term impact on our economic prospects than any form of direct support provided to business. Much more of the inspiration for our economy should be based on the strength and ambition of our cities and their communities. It was this local leadership that built our country in the first place.

- 26.** My preoccupation throughout my years in government and beyond has been to try to transform the competitiveness of the British economy. If we are to do that successfully for the long term, there are two prior conditions.
- 27.** First, our responsibilities as individuals. We cannot overstate the essential role of the individual and leadership. Show me a problem and I will ask first who is in charge. But too often we think of the country's economic problems as something beyond us as individuals – as consequences of tax, regulation or educational standards. We allow the subliminal message to radiate that these are issues for someone else to fix. That is exactly the wrong message. The economic war is relentless and detailed and played out in the decisions taken by millions of British citizens every working day. We all need to raise our game, and keep raising it. All our competitors will.
- 28.** The public sector has a poor record of empowering the individuals in its ranks. By its nature it tends to constrain the essential entrepreneurial spirit within us all. I reject the view, however, that enterprise is a quality found only in the private sector. The headteacher who turns round a sink school and the official who leads the team that secures a billion pound inward investment project, are examples of commendable public enterprise. But too often the demands of bureaucracy sap the innovation and enthusiasm to provide the best and most innovative services. How many MPs have ever considered the impact on the behaviour of civil servants of their insistence that every detail of any decision is recorded so that it can be scrutinised in a parliamentary question? Such a discipline would bring the private sector to its knees.
- 29.** The second precondition for economic transformation is stability. If we are to inject confidence into the economy, we need stability. Investors demand it. They invest against five to 10 year plans and want to know that the rules of the game will not change. The need for certainty about our future relationship with Europe is a prime example. If we are to inject enthusiasm into our business communities to invest their energies into the growth of their local economies they want to be sure that their efforts will not be overtaken by another divergent initiative two years down the line. We therefore need the maximum political consensus possible about the best architecture for promoting growth in the economy. But we must then let that architecture stand the test of time so that all can get on with the real business of creating wealth.

A blueprint for the future

- 30.** All this has led me to conclude that we need a number of significant innovations which, together, will provide a stable yet flexible architecture for the future:
- > a Prime Minister-led National Growth Council, ensuring all parts of government play their part to support growth and with an independent secretariat to ensure its conclusions are fully and expeditiously implemented
 - > a very significant devolution of funding from central government to Local Enterprise Partnerships so that government investment in economic development is tailored directly to the individual challenges and opportunities of our communities, and can be augmented by private sector investment
 - > a clear statement by government of its priorities to guide Local Enterprise Partnerships in the preparation of strategic plans for their local economies
 - > and for central government, a clear policy for each sector of the economy conceived in conjunction with industry and academia.
- 31.** The particular priorities of governments – their economic vision for our country – will change parliament by parliament. The system proposed here can respond to those changing priorities.
- 32.** There are many descriptions used to criticise so comprehensive an approach. Picking winners, intervention. There is one overwhelming response. In their own ways all our competitor economies manage their systems along these lines. We are the ones out of step.
- 33.** It will be said of this report that it is too prescriptive and that cannot be denied. My case is based on the experience of ministerial life and the myriad of reports like this that are littered across Whitehall. Every prime minister of whom I have knowledge has been frustrated by their inability to make Whitehall work effectively. The levers are there but the links are elastic. Pull them and not much happens. We need to link the levers to the gears.
- 34.** The engagement of the devolved administrations during this review has been helpful and enabled us to learn from their experiences. As economic development is devolved to Scotland, Wales and Northern Ireland, much of this report focuses on how the system in England operates. However, the UK Government retains responsibility for many issues which affect the competitiveness of the economy across the UK. A number of recommendations fall into this category.
- 35.** I have also tried to comment only on areas of policy of which I have some knowledge. That leaves significant gaps but even these may be partially filled by the philosophical approach I outline.

- 36.** I acknowledge that there is a strong dose of criticism for many in what I say. This is not because I despair for this country. Exactly the opposite. We have many world class companies of all sizes and four of the world's six best universities. I know how well we can do. We have our history, our culture, our sense of tolerance and fair play, our inventiveness, our ability to laugh at ourselves. It is precisely because so much is so good that I know how much more we can achieve.
- 37.** Britain's relative decline has been long term, far reaching and about averages. Precisely because we still have so much in this country that is world beating we can delude ourselves into thinking that things are not that serious at all. We must not ignore the 30% of UK companies with stagnant growth or turn a blind eye to the sink schools, the forgotten communities and their debilitating impact on society at large. We will only make a difference to our aggregate economic performance if we motivate and excite well beyond that section of our society that is already out in front excelling in the face of the world's most ruthless competitors. We have extremes of industrial, commercial, academic, cultural and sporting excellence. That should encourage us to believe we can raise our game and the average of our national performance.
- 38.** There are no easy or short term ways to beat the world's most competitive economies. The pressures and challenges of an ever more educated, motivated and competitive world are going to intensify. Every sinew of our body politic will need to be stretched simply to keep up. To be good only in part is to lose. We all have to work to be as good or better than them. The real lesson of our Olympic triumph is that four hundred of our fellow citizens pushed themselves for eight long years to the threshold of human tolerance. Government helped. It worked. It was a grand project. We can do it as well as anyone.
- 39.** This report is a challenge to all of us in both the public and private sectors – politicians, business leaders and individuals. We are all responsible for ensuring that the UK creates the wealth upon which our aspirations depend. It is a challenge from which there is no escape.



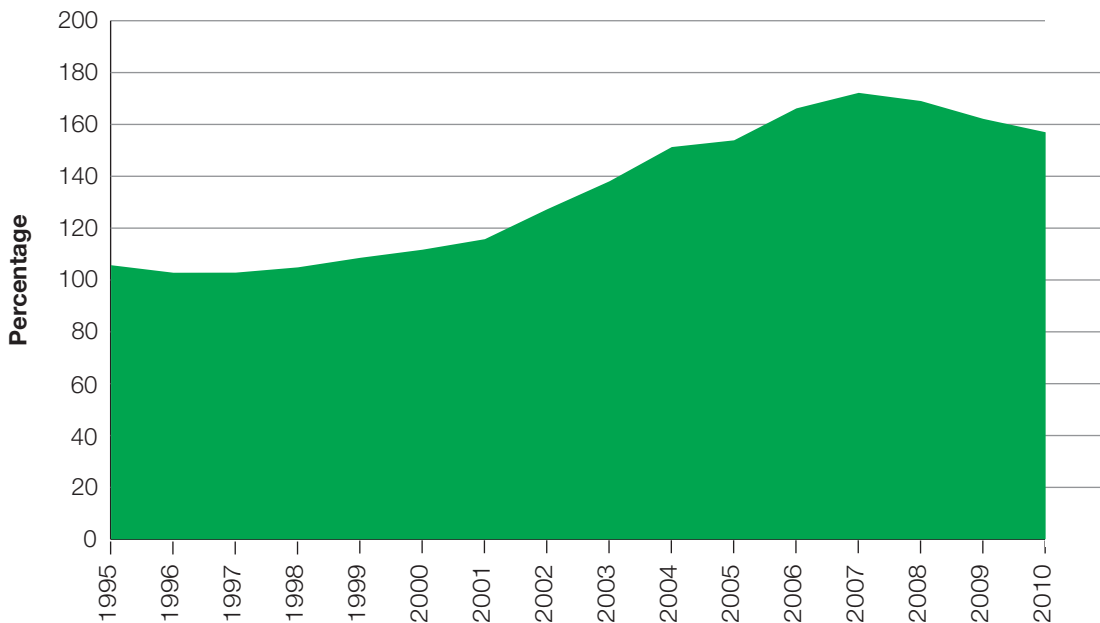
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Chapter 1:

The worst economic crisis of modern times

- 1.1** The economic crisis continues to be the most dominant influence on all our lives. In the UK it drives many of the decisions we make – as individuals, families, communities and as a country.
- 1.2** Times are tough for many households. Inflation has outstripped wage growth for the last four years so the majority of people are feeling the pinch. This has had inevitable consequences for people’s ability and willingness to increase consumer spending.
- 1.3** At a national level, beyond the immediate need to reduce the deficit, governments across the world, for years to come, will continue to shift their focus to living within their means. In the short term this will mean there is very little money for new initiatives. That is why this report advocates a radical rethink as to how we allocate public money in this country to achieve growth.
- 1.4** Many people look back to better times, when our economy boomed throughout much of the 1990s and early 2000s. However, figures show that much of the consumption that led that growth was fuelled by unsustainable levels of debt, both in the public and private sectors, and at household level (see Chart 1.1).
- 1.5** The imperative to rely less on debt may be widely recognised but achieving the change in the public sector is at the frontiers of what democracies can achieve.

Chart 1.1: UK household debt², as a percentage of Gross Disposable Income 1995–2010



Source: OECD³

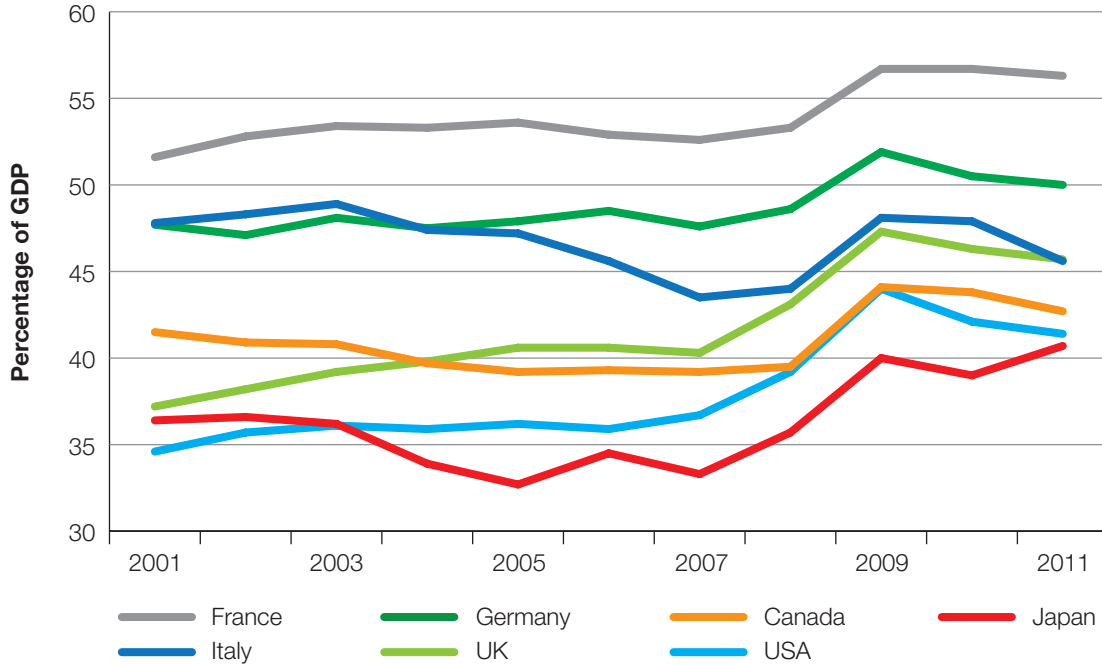
2 Households and non-profit institutions serving households

3 <http://stats.oecd.org/>

- 1.6** We cannot avoid the disciplines of our predicament – from now on levels of spending for government will be constrained by the need to get public sector borrowing under control. Look across the world – there is no other option.
- 1.7** The constraints in public spending enhance the need to achieve private sector growth across the country. It is the proceeds of growth – individual and national – that can increase our standard of living to the levels to which we aspire.
- 1.8** There are many reasons to explain the recent stagnation in our economy. One of the most important seems to be lack of confidence. Uncertainties in our economy and around the Eurozone are holding back investment decisions in the immediate term. Much of the evidence suggests that many of our businesses are sitting on cash, although the SME sector has particular problems with accessing finance.
- 1.9** This must not, however, divert our attention from the UK's long term economic opportunities. The squeeze on finances domestically, and in the economies of many of our competitors, disguises the fact that some countries currently continue to see attractive levels of growth. This in turn generates unprecedented additional annual demand in those economies for goods and services. As the rest of the world gradually recovers from recession, that outlook will only get rosier. Put simply – there are over seven billion people out there with their total global income growing by around 2.9% or some US \$2.1 trillion per year⁴.
- 1.10** Interwoven with this historic shift to emerging economies has been the advent of highly educated middle classes, informed by international news services, personal communication technologies serviced by the internet and at least familiar with the English language. The Arab spring had all the elements of copycat protest spreading frustration from country to country. Fortunately much else of a less violent nature is spreading across the world to create a market place of unprecedented scale. The bottom line is there is much to go for.
- 1.11** As Chart 1.2 shows, the Government will itself remain an influential contributor to our national wealth. All projections about future levels of public spending, even after austerity measures are factored in, show it remaining at a broadly similar level as today. How the Government spends this money can in itself be a significant factor in encouraging growth.

4 Based on (i) US Census Bureau 'World POPClock Projection' www.census.gov/population/popclockworld.html and (ii) 2013 projection of growth in Value of World Output at market exchange rates from IMF *World Economic Outlook: Coping with High Debt and Sluggish Growth*, October 2012

Chart 1.2: General government expenditure (as a % of GDP) G7 economies 2001–2011



Source: IMF World Economic Outlook Database⁵

1.12 There can be no dispute about the urgent need to get the British economy back on track. I believe the Government’s economic strategy is right. However, there are many ways in which we could use existing levels of expenditure more effectively and, in particular, in ways that attract additional non-government funding. My experience with urban grants, Urban Development Corporations, City Challenge and the Regional Growth Fund demonstrates the effectiveness of using limited public money to leverage greater additionality from the private sector. It shows, in essence, that we can make every penny of taxpayers’ money go further.

1.13 If there is an upside to the recent crisis it is that it has encouraged a wide and shared interest in securing our longer term competitiveness and growth. Businesses will not make new investments on the back of short term policy initiatives – they need confidence in the long term competitive strength of our economy. International economic competition will only intensify.

1.14 The International Monetary Fund (IMF) projects that the real GDP of developing economies will grow at just over 4% each year to the end of 2016⁶, compared to just 1.3% annually in advanced economies. At these growth rates an additional US \$11.3 trillion of real GDP will have been generated in emerging markets over the four year period to the end of 2016, compared to \$6 trillion in advanced markets. Many look at these figures and urge us to put all our efforts into trading with the BRICS – Brazil, Russia, India, China and South

5 www.imf.org/external/pubs/ft/weo/2012/01/weodata/index.aspx

6 IMF, *World Economic Outlook: Coping with High Debt and Sluggish Growth*, October 2012

Africa. But we cannot be competitive in new markets if we are not first being leaders in the markets in which we have been operating for years.

1.15 To compete properly, and win, we need to understand fully what we are good at and where we need to improve. We have over decades done many things better than our rivals, but not everything. The pursuit of growth must not be an accidental occurrence – it needs to be underpinned by a comprehensive analysis of our strengths and weaknesses. By recognising where we are strong and building on it, whilst understanding where we are weak and tackling it, we can develop an agenda relevant to the competition we face.

1.16 The observations ahead are a summary of a thorough analysis and international benchmarking exercise undertaken to inform this review⁷.

Many headline strengths in the UK economy

1.17 The most recent Global Competitiveness Report from the World Economic Forum⁸ ranks the UK as the eighth most competitive country in the world in which to conduct business, up two places over last year. This reflects the UK's strong performance on entrepreneurial activity and inward investment. In terms of new business start-ups the UK outperforms many G7 countries including Germany and France although we still trail the US and other international competitors⁹. The UK is second only to the US in the value of foreign direct inward investment it attracts¹⁰.

7 For detailed discussion and data see BIS, *Benchmarking UK Competitiveness in the UK Economy*, BIS Economics Paper No. 19, 2012. <http://www.bis.gov.uk/assets/biscore/economics-and-statistics/docs/b/12-1207-benchmarking-uk-competitiveness-in-the-global-economy>

8 World Economic Forum, *The Competitiveness Report 2012-2013*, 2012 http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2012-13.pdf

9 *Global Entrepreneurship Monitor UK Report*, J Levie and M Hart, 2008 and *Global Entrepreneurship Monitor UK Report*, J Levie and M Hart 2011

10 UNCTAD, *World Investment Report*, 2012

Table 1.1: International rankings of competitiveness, 2012

Ranking	WEF Global Competitiveness Report	IMD World Competitiveness Year Book	World Bank Doing Business Ranking
1	Switzerland	Hong Kong	Singapore
2	Singapore	United States	Hong Kong
3	Finland	Switzerland	New Zealand
4	Sweden	Singapore	United States
5	Netherlands	Sweden	Denmark
6	Germany	Canada	Norway
7	United States	Taiwan	United Kingdom
8	United Kingdom	Norway	South Korea
9	Hong Kong	Germany	Georgia
10	Japan	Qatar	Australia
United Kingdom (18)			

Source: IMD, WEF (2012), World Bank (2013)

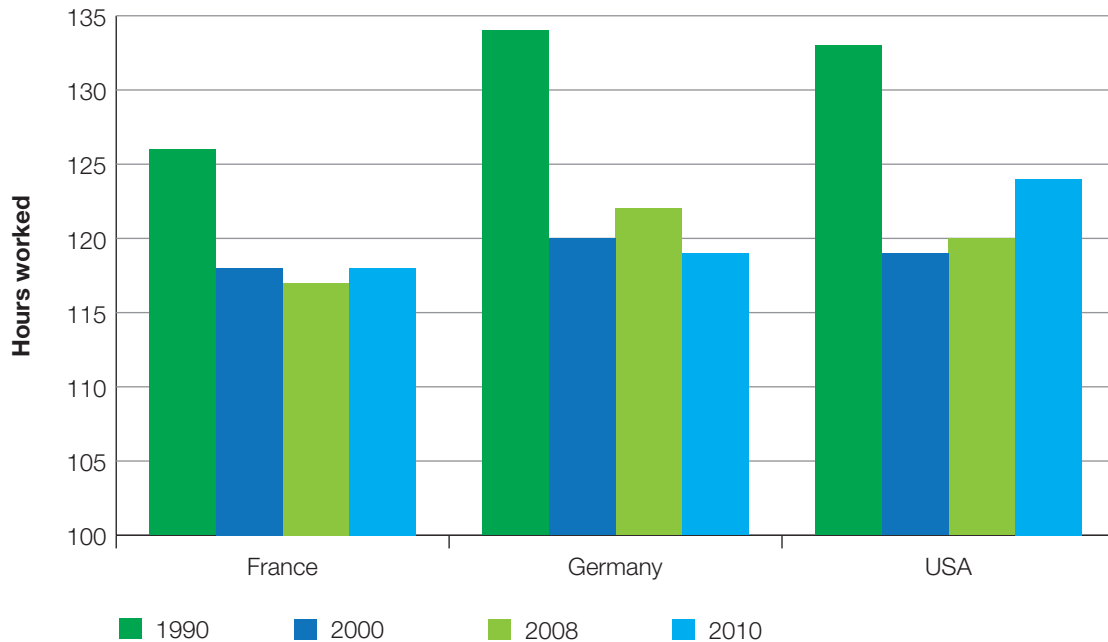
- 1.18** Alternative measures of international competitiveness place us both higher and lower in the world’s league table. So depending on which analysis you choose to look at, and which measures you opt to quantify, the UK’s relative performance varies widely. Competitiveness is not a precise measure – it is a complicated mix of many, often unquantifiable, factors. In order to raise our game we must improve our performance across the board.

What we do well and what we do not do so well

The productivity gap

- 1.19** The UK has made significant progress narrowing the longstanding productivity gap with our peers.
- 1.20** But most significantly for our long term economic prospects, UK output *per hour worked* – as shown in Chart 1.3 – still lags behind that of our international trading partners in the US, Germany and France.

Chart 1.3: Relative GDP per hour worked (UK = 100)



Source: ONS International Comparisons of Labour Productivity

1.21 This gap is apparent across most sectors of our economy, but especially in manufacturing. Based on these measures the average UK worker has to work 10 hours to produce the same output that a worker in the US could produce in eight. How much more productive would we be in the UK if we enabled UK workers – through investments in skills, infrastructure, capital equipment and R&D – to be as productive per hour as our leading competitors? This is not just about working harder, but about being more productive with the time we put in.

Gross domestic product

1.22 The UK saw average annual GDP growth of 2.2% between 1990 and 2008 – placing it third in the G7, behind only the US and Canada¹¹ (see Table 1.2). Based on our historical performance a return to similar rates of growth could see the UK outstrip most of our competitors.

1.23 But these figures hide a problem. Historically, and prior to the financial crisis of 2008, growth was increasingly driven by the accumulation of unsustainable levels of public and private sector consumption fuelled by debt, greatly outstripping the contributions of business investment and net trade to UK economic growth. Net trade had an increasingly negative impact as our demand for imports grew at a faster rate than our ability to export.

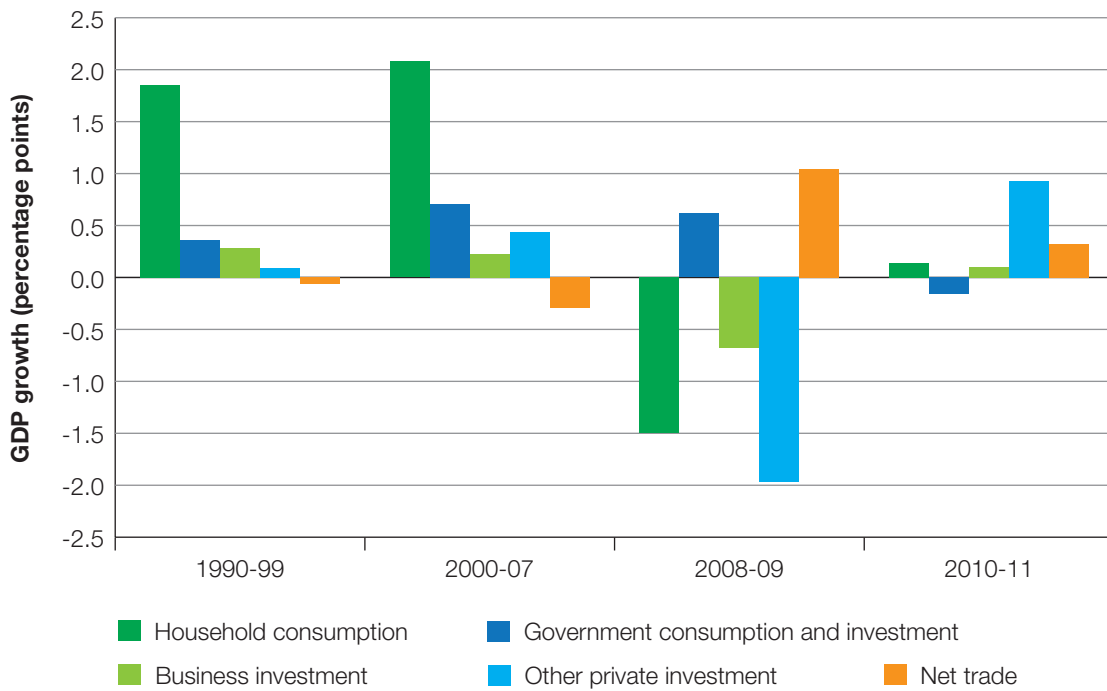
¹¹ OECD, *National Accounts Statistics*, 1990-2011 data

Table 1.2: Average annual GDP growth, G7 economies, 1990–2008

US	2.45%
Canada	2.40%
UK	2.21%
France	1.54%
Germany	1.53%
Italy	0.96%
Japan	0.85%

Source: BIS calculations based on OECD data

Chart 1.4: Average annual contributions to UK GDP growth

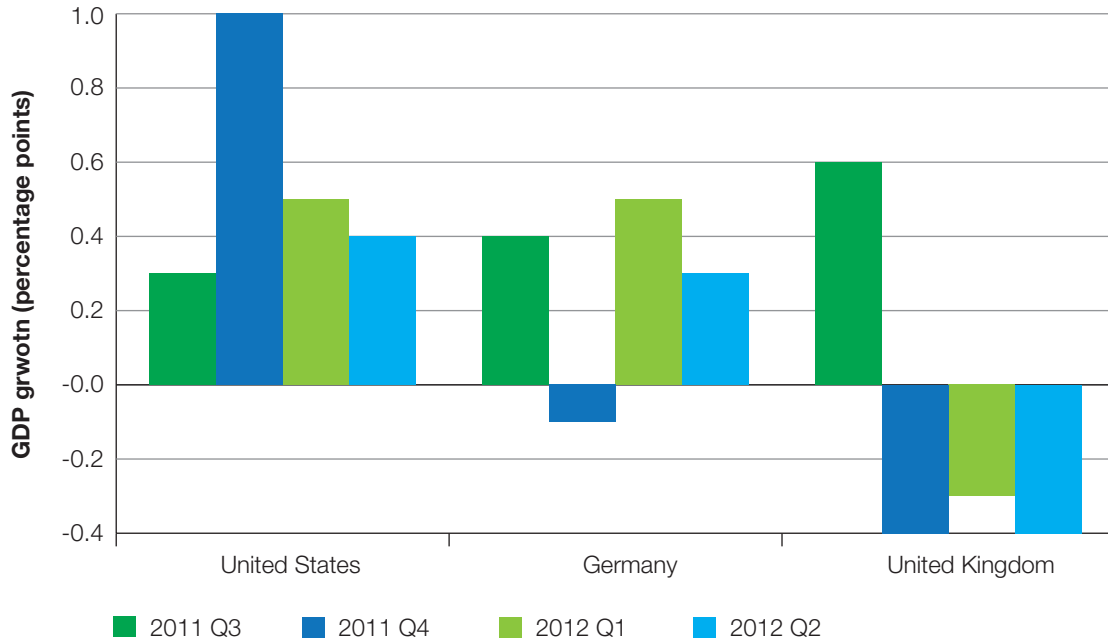


Source: BIS calculations based on ONS National Accounts

1.24 Although some indicators, particularly falling levels of employment, provoke the question about the reliability of these statistics the broad message remains the same. It has now been confirmed that we are experiencing a double dip recession with output shrinking in each of the last three consecutive quarters. As Chart 1.4 shows, output shrank by 0.4% in the second quarter of this year while Germany and the US continued to experience positive, albeit modest, growth in their economies¹².

¹² ONS, *National Accounts*, 2012 and OECD, *National Accounts*, 2012

Chart 1.5: Quarterly GDP growth, selected countries 2009–2012



Source: OECD National Accounts

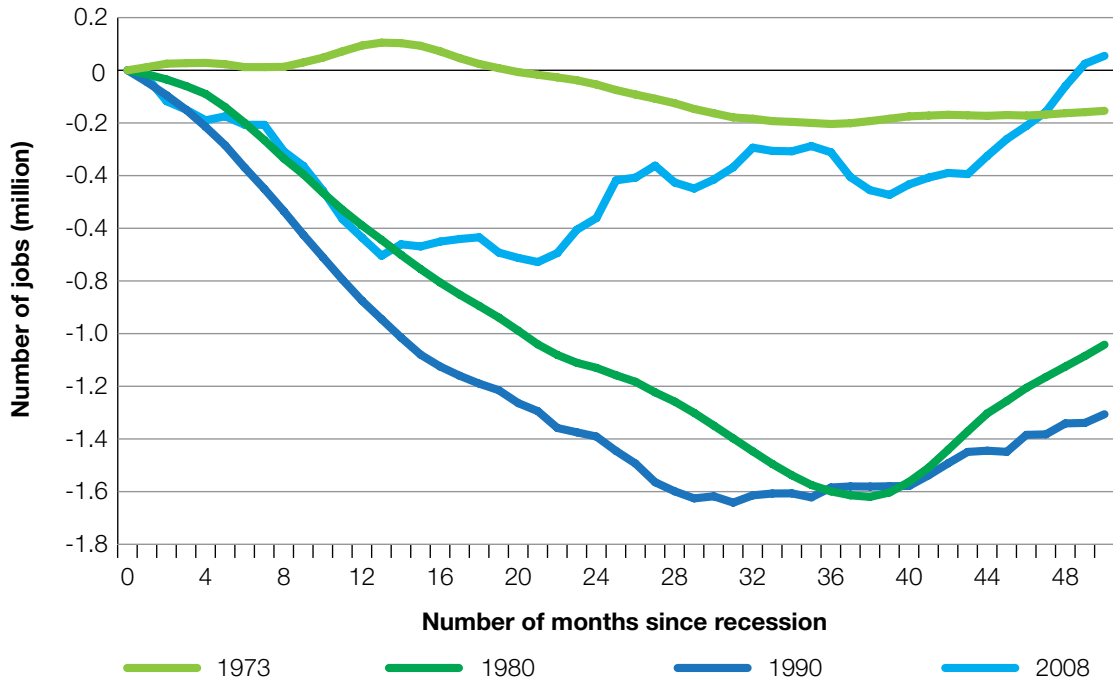
1.25 The IMF has also revised down its forecasts for the UK economy predicting it will shrink by 0.4% overall this year and grow by only 1.1% next¹³.

Employment

1.26 Unemployment, particularly youth unemployment, remains high. While that rightly gives us cause for concern, the fact is it remains at a level about one million lower than originally forecast. In the past, the first reaction of many firms to a downturn would be to lay people off (see Chart 1.6 and Table 1.3). What we have seen in this recession is a more flexible approach from employers and employees alike. Many companies have kept staff on and instead renegotiated their terms, having the foresight to recognise that their skills and knowledge will be essential to the firm’s future growth.

¹³ IMF, World Economic Outlook, 2012 data

Chart 1.6: Change in UK employment following past recessions



Source: ONS, Labour Market Statistics, ONS¹⁴

Table 1.3: Change in UK employment following past recessions

Year	Qtr	Unemployment at peak (rate%)
1977	Q3	1.5 million (5.7%)
1984	Q2	3.27 million (11.9%)
1993	Q1	3.00 million (10.6%)
2008	Q4	2.66 million (8.4%)

Source: ONS, Labour Market Statistics¹⁵

Research and development

1.27 Of clear note is the UK’s strong reputation for world class research, ranking second only to the US in terms of most influential publications. However, when it comes to translating that research into goods and services we remain below average on measures such as research and development intensity – the level of profits our companies reinvest back into research and development – and the extent to which we commercialise our discoveries¹⁶.

¹⁴ www.ons.gov.uk/ons/datasets-and-tables/

¹⁵ Ibid

¹⁶ OECD, *Science Technology and Industry Outlook*, 2010

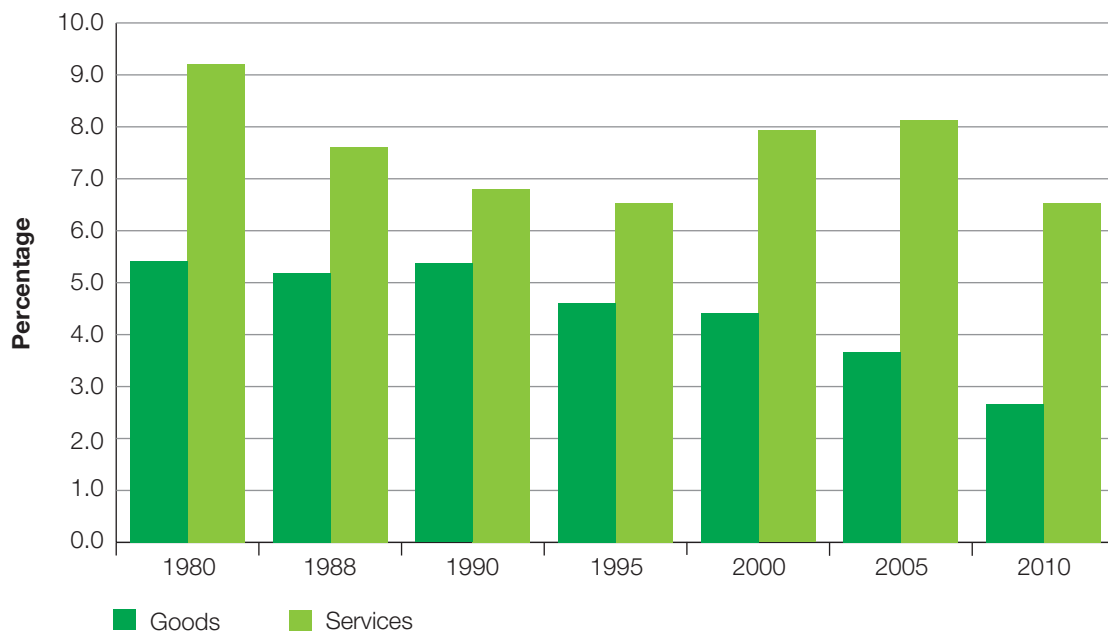
Our universities

1.28 Similarly, the UK has a relatively strong higher education sector even though other countries continue to make ambitious investments. We have four of the six best universities in the world¹⁷. Despite this, skills gaps are too wide at the intermediate and basic levels, including in maths, literacy and science. UK industry also appears to be relatively less skills intensive and employs fewer graduates in professional and technical occupations than its major competitors¹⁸. No boom in growth can be achieved without a significant rethink as to how we develop skills in this country – both funding training and its delivery.

Trade in goods and services

1.29 Over the last 30 years the UK's balance of trade and share of global export markets have deteriorated (see Chart 1.7 below), although these trends are shared with many other advanced economies.

Chart 1.7: UK share of global exports, 1980–2010



Source: BIS calculations based on World Trade Organisation (WTO) data

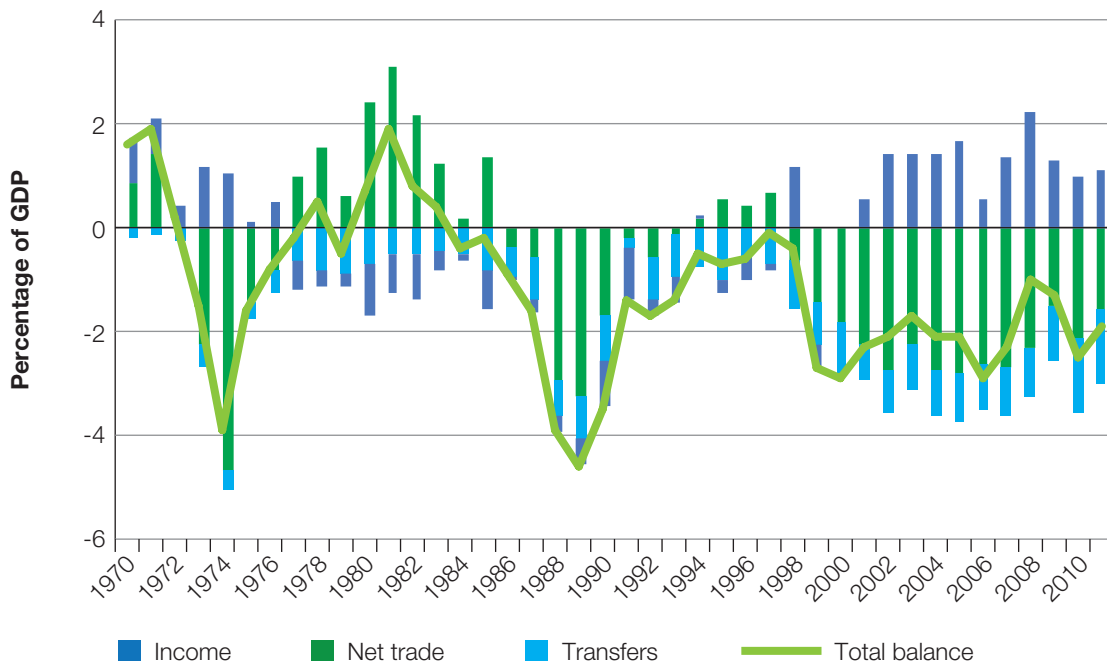
¹⁷ QS World University Rankings, 2012

¹⁸ OECD, *Education Statistics*, 2010

1.30 The relative decline in our export performance has been driven predominantly by a reduction in our share of global exports of goods. We are now only the 10th largest exporter of goods, falling behind Italy. Although we have a number of areas of relative specialisation in areas such as specialist textiles, engines and turbines, our export performance tends to be weak across general manufacturing sectors. Whilst we remain the second largest exporter of services overall, our share of the global market has been squeezed from over 5% in 1980 to under 3% in 2010¹⁹.

1.31 The UK current account deficit – broadly the amount we buy in goods and services from abroad compared to the amount we sell – has remained high. The latest data shows that the UK ran up a record current account deficit of £20.8 billion in the second quarter of this year, equal to 5.4% of GDP²⁰. But this is not a new phenomenon – as Chart 1.8 shows – we have remained in deficit for many years.

Chart 1.8: UK current account balance (as a % of GDP) 1970–2011



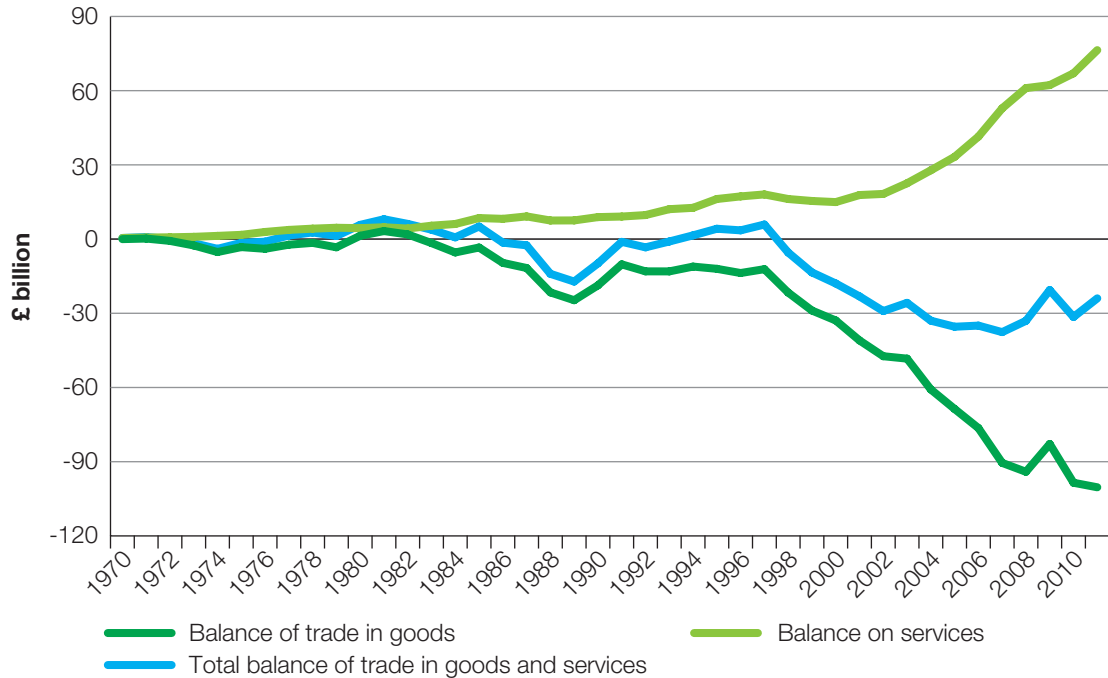
Source: ONS Balance of Payments Quarterly First Release Q1 2012

1.32 We must address these issues. An analysis of the trade gap shows a stark contrast between our balance of goods and our balance of services.

¹⁹ BIS calculations based on World Trade Organisation Statistics, International Trade Centre Statistics and IMF World Economic Outlook Statistics, 2010 data

²⁰ ONS, *Balance of Payments Statistics*, 2012 Q2 data

Chart 1.9: UK balance of trade in goods and services, £ billion 1970–2011



Source: ONS Balance of Payments Quarterly First Release Q1 2012

1.33 While the surplus in the balance of trade in services has grown steadily, it has been outgrown by the rise in the trade deficit in goods. So the question arises – with imports outweighing exports – how do we pay our way in this country?

Table 1.4: UK balance of payments, £ million 2011

Current Account		-29,002
<i>Of which</i>	<i>Balance of trade in goods</i>	<i>-100,014</i>
	<i>Balance on services</i>	<i>76,305</i>
	<i>Balance on income</i>	<i>16,849</i>
	<i>Net current transfers</i>	<i>-22,142</i>
Capital Account		3,444
Financial Account		15,997
Net errors and omissions		9,561

Source: ONS Pink Book 2012

- 1.34** It should be noted that these balance of payment figures are based on cash accounting. A significant element of financial accounting indicates the extent to which a largely capital inflow is sustaining our international trading position.
- 1.35** If UK growth is not better balanced, with a greater role for private sector investment and exports, we will not be able to take advantage of global market opportunities and respond effectively to ever stronger international competition.

Balance of Payments

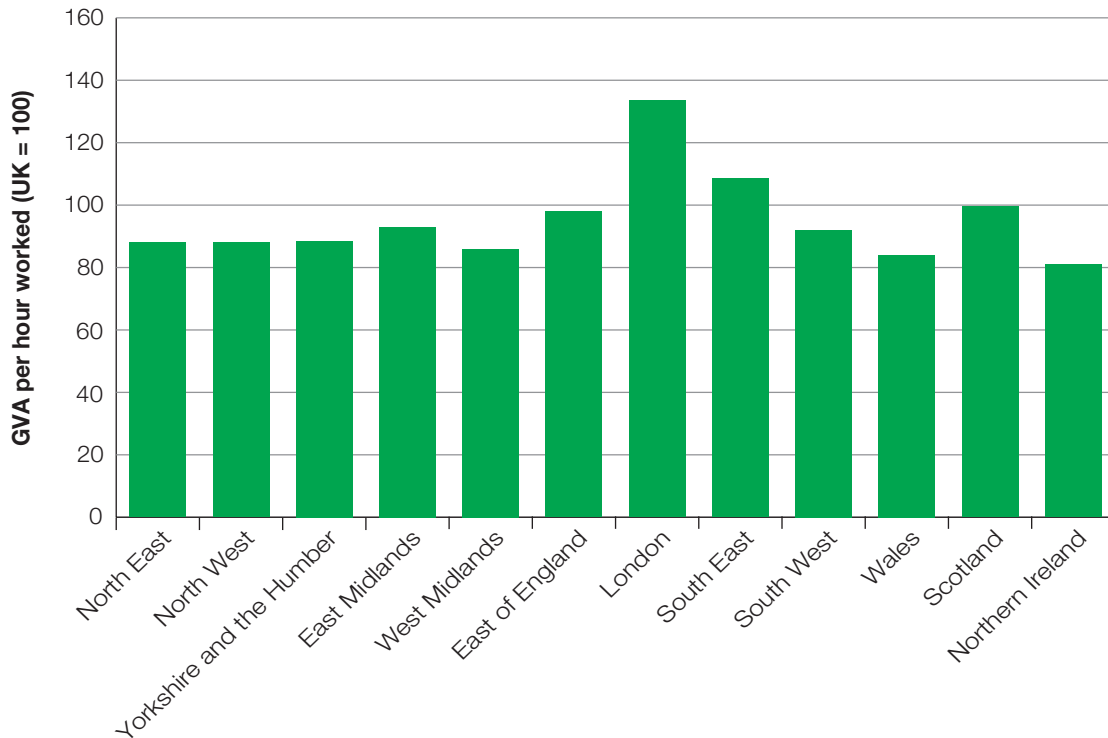
The UK balance of payments measures economic transactions between UK residents and the rest of the world. The main components are as follows:

- (i) The **current account** covering:
- > exports and imports of goods, such as oil, agricultural products, other raw materials, machinery and transport equipment, computers, white goods and clothing
 - > exports and imports of services such as international transport, travel, financial and business services
 - > income flows, such as the compensation of employees paid to non-resident workers or received from non-resident employers, and interest, dividends and profits accrued on external financial assets and liabilities
 - > current transfers include general government current transfers, for example transfers related to international aid and cooperation between governments, payments of current taxes on income and wealth, and other current transfers across international borders, such as pensions, insurance premiums and charitable donations.
- (ii) The **capital account** comprising acquisitions, disposals or transfers of non-produced, non-financial assets including land, buildings, intellectual property and equipment. It also records the cancellation of debts between the UK and the rest of the world and the transfer of goods and financial assets by migrants leaving or entering the UK and any payments of gifts and inheritance taxes they may make.
- (iii) The **financial account** comprising transactions associated with changes of ownership of the UK's foreign financial assets and liabilities including direct investments, investment in shares, debt securities, loans and deposits.
- (iv) **Net errors and omissions.** The difference between the sum of credit and debit entries to the balance of payments must be zero. In practice, some transactions are not measured, for example, due to omissions or time lags in the receipt of data, or are measured inaccurately. Data used to compile the accounts also comes from a wide variety of different sources which may not be consistent. Therefore, to restore the equality of credit and debit entries, a net errors and omissions item is included.

Persistent regional disparities

1.36 Despite the efforts of successive governments to address regional disparities, the variation in economic performance across the UK persists.

Chart 1.10: Regional GVA per job, 2010

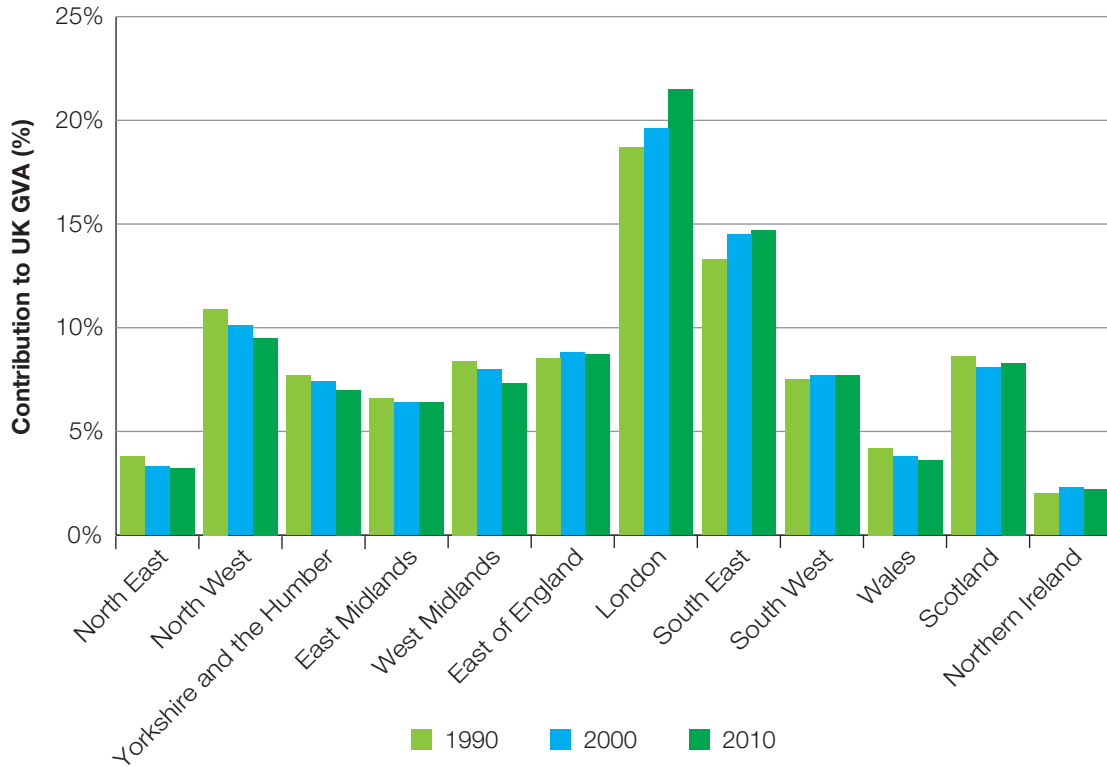


Source: Regional, sub-regional and local Gross Value Added, ONS 2011

1.37 It is not surprising that London contributes more to the UK economy than any other region in the country. London occupies what is arguably a unique position amongst world cities. It is possible to argue in favour of Washington DC as the most powerful political centre, or New York as the largest financial centre, or Paris as the most cultural, but there is no city that combines such a depth of political and commercial influence with such a depth of historic and cultural provision. London is unique and a national asset of incalculable value. Every policy should encourage it on.

1.38 However, more than 50% of Gross Value Added (GVA) now comes from outside London and the South East, while there has been a relative decline in the contribution to GVA by the North and the Midlands over decades (see Chart 1.11). It is not the relative difference between the contributions of different regions that matters most but the ability of all regions to grow their wealth and prosperity.

Chart 1.11: Regional contributions to UK GVA, 1990–2010



Source: BIS Analysis of ONS Regional Gross Value Added, ONS 2011

1.39 London will always be an important factor in the economic prosperity of the whole of the UK. However, its success should not be at the expense of the rest of the country. Nothing that I say in this report is intended to see London held back – exactly the reverse. My proposals are designed to help all regions innovate, grow and increase their absolute wealth.

1.40 By focusing on raising our performance in every town and city we will return our economy to sustained, long term growth.

1.41 What is clear to me, whether we adopt a sectoral approach or a more local, place based approach, is that growth is everyone’s business. Government can set national policies and create an environment where business can flourish, but success depends on businesses and individuals, working together.

1.42 As we prepare for growth we must – each and every one of us – do all in our power to advance it. It is not someone else’s problem.

Chapter 2:

Localism - building on our strengths

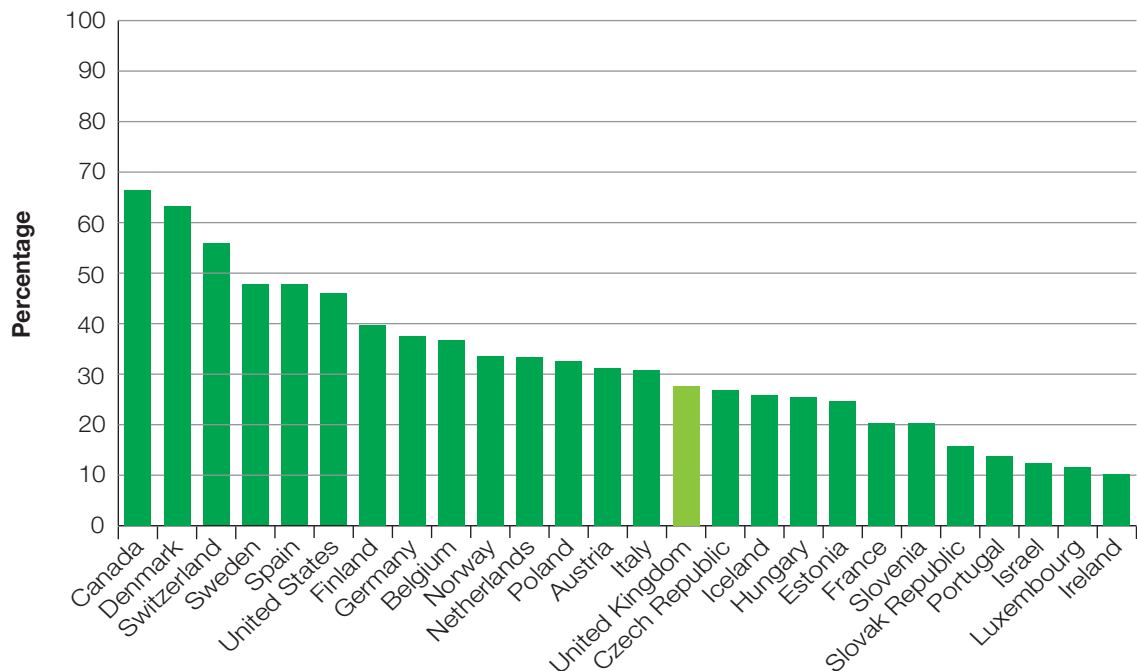
The drift to centralism

- 2.1** The grand Victorian town halls of Birmingham, Bradford, Liverpool and Manchester attest to an age when people looked to their city, and not just to Westminster, for solutions. Powerful local government held sway, led by business people who applied their entrepreneurial energies to the economic development of their communities.
- 2.2** Those days are gone. Industrialisation demanded migration and urbanisation. In the absence of basic infrastructure the ever expanding cities were unable to cope with the ensuing overcrowding and disease. People were living in unacceptable conditions. It fell to local government to respond to the needs and demands of the ever growing electorate.
- 2.3** The cost of providing the necessary infrastructure and basic social support could not, however, be borne by many of the cities themselves. Wealth had to be redistributed by central government. And with that redistribution came central controls. Power and initiative shifted from provincial England to London and its bureaucracies – a process that has now continued almost without check for over a century.
- 2.4** With central government reserving for itself the power to make the vast majority of economic decisions – creating itself as a functional monopoly – local authorities have been relegated to service providers. To make matters worse, as Whitehall has taken more powers so its distrust of local decision makers has increased. At the first sign of trouble, further powers are wrested back to the centre. At the same time – and I would say as a result – the involvement of local business people in the governance of their communities has dwindled, and their energy and innovation has been lost. The local economic leadership that drove the UK to the forefront of the world economy has disappeared.
- 2.5** Besides neutering local leadership, the monopoly of Whitehall is dysfunctional on two counts. First, too many decisions are taken in London without a real understanding of the particular, and differing, circumstances of the communities affected. And second, with responsibilities divided up between policy departments, no one in government is tasked to look holistically at the full range of issues facing a particular area.
- 2.6** The economic challenges faced by Bristol, Cambridge or Hull will never be fixed simply by improving housing or upgrading broadband access. Barriers to growth are always multi-faceted. But Whitehall continues to approach these issues from the individual policy priorities of different departments, as if economic issues can be addressed effectively in a placeless vacuum. All my experience with place based initiatives – from Urban Development Corporations to City Challenge and the Regional Growth Fund – tells me there is a better way.

Other countries have more devolved systems of government

2.7 As a country, we have a high degree of centralisation in our system of government. Many other OECD countries devolve greater powers and spending to tiers of state, regional or local government. As Chart 2.1 shows, in the UK around 30% of public expenditure is spent by local government. Compare this to countries with political traditions as diverse as the US and Sweden where almost 50% of all public expenditure is accounted for by their state and local governments. In Canada and Denmark it is nearer to 70%.

Chart 2.1: International comparison of the percentage of general government expenditure spent by sub central government (2010)



Source: OECD National Accounts

Complexity of local government

2.8 Not only have we disempowered local government by centralising power and funding, but the English system of local government remains overly complex and inefficient.

2.9 This complexity has long been recognised. England of the 1960s had 1,400 local authorities with an attendant array of aldermen and municipal glory. Following the Royal Commission on Local Government in England 1966–1969, the Redcliffe-Maud report²¹ recommended the comprehensive streamlining of local government based around unitary local authorities.

²¹ Redcliffe-Maud chaired a Royal Commission on Local Government in England between 1966 and 1969 which published a report and recommendations for reforming the structure of local government in England outside London.

- 2.10** Redcliffe-Maud recommended introducing a new system of 58 single authorities and three metropolitan areas based on what could loosely be called the city state model. I served with Peter Walker in the newly created Department of Environment in 1970 charged with taking forward the report's conclusions. The politics were dreadful with constituency activists and local councillors refighting the battles of English history to preserve a status they felt to be inherent to world stability. Peter painfully steered a reduction of the 1,400 authorities to around 400. I was part of the infantry criss-crossing the country encouraging angry councillors to accept the brave new world.
- 2.11** Today, England has 353 principal authorities. Some of these are single unitary authorities, others operate in tiers of district and county councils. The number of different councils doing similar things remains costly and confusing. For many, the range of different systems is baffling too. Scotland and Wales, on the other hand, both have a system of single unitary authorities with clear accountability and responsibilities.
- 2.12** In addition, the boundaries of many English local authorities bear no relation to modern patterns of economic activity – they are not functional economic market areas (FEMAs). This adds to the difficulties local authorities have in understanding what decisions are needed for their economies and limits their ability to take the action needed for local growth.

What is a functional economic market area?

Functional Economic Market Area (FEMA) is a term economists use to describe the functional area over which the local economy and its key markets operate. So not just where businesses are located, but where their staff live and suppliers come from.

There is no universal approach to defining FEMAs. A city's labour market area, for example, is unlikely to have similar boundaries as key supply chains or the areas within which consumers access key goods and services. Ideally, FEMAs are recognised on the basis of several markets or catchment areas which best reflect the drivers of the local economy.

- 2.13** Overall, the English system of local government is not suited to the demands of the 21st century and in particular our need to pursue economic growth.

Stimulating local growth

- 2.14** For the UK to face up to the challenge of increasing international competition, we must reverse the long trend to centralism. Every place is unique. Local leaders are best placed to understand the opportunities and obstacles to growth in their own communities. Policies that are devised holistically and locally, and which are tailored to local circumstances, are much more likely to increase the economy's capacity for growth. National policies devised by central government departments can never be as relevant to all the different circumstances of our local economies as strategies that originate in those places to start with.
- 2.15** My proposals are in two parts. First, we need to empower local places by letting them take the initiative to generate local growth, in partnership with central government. With initiative will come responsibility. And second, we must ensure that the incentives and structures of local places are organised in such a way as to secure the greatest possible economic contribution, with each area able to play to its natural strengths.

Previous policies to stimulate local initiative

- 2.16** Over my career I have had the privilege of leading a number of initiatives which have created local partnerships, bringing together disparate organisations in a shared endeavour to tackle local issues. In 1979 I inherited the urban grant mechanism from the Labour Government. I changed just one condition. To secure a grant, I insisted that local government had to link up with private sector partners in the implementation of a particular scheme. For example, to get a grant to clear toxicity from a derelict site and use it for housing they had to join with a builder.
- 2.17** In 1979 I launched the concept of the Urban Development Corporation (UDC) which led to a total of 13 being established²². UDCs established the foundations for London's Docklands and were at the heart of a renaissance in several of our cities.

²² Birmingham Heartlands, Black Country, Cardiff, Langanside, Merseyside, Plymouth, Sheffield, Teesside, Trafford Park, Tyne & Wear, Thurrock Thames Gateway, London Thames Gateway and West Northants

Urban Development Corporations (UDCs)

A total of 13 UDCs were established in England with the objective of securing economic regeneration in their localities. The lifetime of projects varied from five years (Plymouth) to 17 years (London Docklands).

A study of eight UDCs* showed that their total expenditure was estimated at £2.37 billion. Individual corporations' total spending varied from around £60 million for Plymouth and Birmingham Heartlands to over £400 million for Merseyside, Tyne & Wear, Teesside and the Black Country. UDCs were also very effective in leveraging private sector investment. The average leverage rate was approximately £2.75 for every £1 of public money invested.

The UDCs resulted in:

- > 138,266 gross jobs created
- > 322 km of roads providing improved infrastructure
- > 4,790,534 square metres of commercial floorspace created
- > 11,478 housing units developed.

*Birmingham Heartlands, Black Country, Merseyside, Plymouth, Sheffield, Teesside, Trafford Park and Tyne & Wear.

- 2.18** In 1990 I introduced City Challenge. In total, 31 City Challenge partnerships ran in deprived urban areas between 1992 and 1998.
- 2.19** These schemes paved the way for further regeneration programmes, such as Neighbourhood Renewal and the New Deal for Communities. More recently I have chaired a committee to advise the Government on its £2.4 billion Regional Growth Fund (RGF). The Fund aims particularly to help those areas and communities which were dependent on the public sector to make the transition to sustainable private sector led growth and prosperity. In the three rounds to date, 306 bids were successful with a conditional allocation of £2.4 billion to create and safeguard 570,000 jobs. For every £1 of public funding it has levered an additional £6 of private sector investment.

City Challenge

The City Challenge aimed to regenerate specific run-down inner city areas and improve the quality of life for local residents.

Local authorities, in partnership with private, public and voluntary sector organisations and the local communities, were invited to develop a comprehensive strategy for sustainable regeneration in areas of deprivation and to bid for resources to implement this strategy.

Each partnership was eligible to bid for £37.5 million over five years resulting in a total of £1.14 billion of public expenditure.

The collaborative nature of these partnerships meant that they were particularly effective in leveraging other sources of co-investment. For every £1 of City Challenge investment a further £3.78 of private sector funding was sourced and an additional £1.45 from other public sector partners.

The City Challenge Programme resulted in:

- nearly 170,000 gross new permanent jobs created or safeguarded in areas of employment scarcity
- over 110,000 dwellings built or improved
- almost 4,000 hectares of land reclaimed or improved
- over 3.6 million square metres of business space created or improved
- 8,700 businesses started.

2.20 All these programmes show how government funding for economic development can be augmented by the private sector and other partners. Even more importantly the programmes encouraged local partnerships and cooperation with all the consequential benefits for the local economy.

Current policy

2.21 This government has recognised the importance of re-empowering local communities to unlock growth. Several important steps have been taken already.

- **Local Enterprise Partnerships** – 39 LEPs have now been endorsed by government (see box overleaf).

Local Enterprise Partnerships

In June 2010 the Government invited local business and civic leaders to come forward with proposals for establishing LEPs that reflected natural economic geographies.

Thirty-nine LEPs cover the whole of England. LEPs bring local business and civic leaders together to provide the vision and leadership to drive sustainable economic growth and create the conditions to increase private sector jobs in their communities. They cover areas intended to relate to functional economic market areas so their work can build on local strengths, in rural as well as urban areas, and identify the local barriers to growth.

Local areas have considerable discretion about the composition of LEPs, provided they are chaired by a business person and at least half their members are from the private sector.

The Government has recently reaffirmed its commitment to LEPs with significant announcements for funding to support their ongoing function and the help they provide to local SMEs. This month the Deputy Prime Minister announced the results of Round Three of the Regional Growth Fund. The £1 billion of public money included over £300 million for LEPs to administer to SMEs. This represents a strong sign of support that the Government and the private sector increasingly see LEPs as central to the development of their own local business environment.

- > **Growing Places Fund** – £730 million for England has been allocated to LEPs to provide them with funding so they can boost economic growth – building new homes, creating jobs and restarting stalled projects. LEPs are working with both public and private sector partners to identify eligible projects and leverage their allocated funds.
- > **City Deals** – Eight deals were concluded earlier in 2012 with Birmingham, Bristol, Leeds, Liverpool, Manchester, Newcastle, Nottingham and Sheffield. The different deals give England's largest cities major new powers to invest in growth, deliver skills and jobs, support local businesses, control budgets and deliver critical infrastructure. They are helping cities exercise their independence and, through tailored agreements, meet their own local challenges.
- > **Rural Growth Networks (RGN)** – £15 million has been allocated to LEPs and local authorities to support sustainable economic growth in rural areas. RGNs are networks of enterprise hubs which encourage and support entrepreneurship by providing training, knowledge transfer and mentoring. Five RGNs will be established in 2012/13 in Cumbria, Devon and Somerset, Durham and Northumberland, Coventry and Warwickshire, and Swindon and Wiltshire.

- > **Regional Growth Fund** – A £2.4 billion fund operating across England from 2011 to 2015. It supports projects and programmes with significant potential for economic growth that can create additional, sustainable private sector employment.
- > **Enterprise Zones** – Twenty four zones have been created across England to attract new investment and create jobs. Benefits include 100% business rate discounts, simplified planning, provision of superfast broadband, 25 year retention of business rates and, in some areas, enhanced capital allowances.
- > **New Homes Bonus** – This provides additional funding as an incentive for building new homes by match funding the additional council tax raised for new homes and empty properties brought back into use for the next six years.
- > **Community Infrastructure Levy** – A new levy that local authorities in England and Wales can choose to charge on new developments. The money can be used to support development by funding infrastructure that the council, local community and neighbourhoods want.
- > **Business Rates Retention** – The Local Government Finance Bill, currently before Parliament, will provide for local retention of business rates from April 2013. This will enable councils to keep a proportion of the business rates generated in their area, giving them a financial incentive to promote local economic growth and providing them with more control over their own funding streams.
- > **Tax Increment Financing** – The same Bill also proposes to allow for the use of Tax Increment Financing from 2013. This will allow local authorities to use anticipated future tax receipts to support upfront investment in their local area, using their prudential powers.
- > **Devolving Local Major Transport Schemes** – Local major transport schemes have traditionally been approved and funded individually by central government under a centralised bidding process. The Government recognised the importance of transport to local economies and that LEPs are well placed to understand how transport investment can be used to boost economic recovery and growth. As a result, the Department for Transport envisages LEPs playing a key role within the proposed Local Transport Bodies, along with local authorities and other stakeholders, in prioritising and funding key infrastructure projects in a new devolved system from 2015.
- > **The London Legacy Development Corporation** – A Mayoral Development Corporation responsible for the regeneration legacy from the London 2012 Games. It will promote and deliver physical, social, economic and environmental regeneration in the Olympic Park and surrounding area.
- > **Reform of the planning system** – A series of measures aimed at supporting businesses, developers and first-time buyers, while reducing unnecessary red tape across the planning system.

> **Community budgets** – These give local public service partners the freedom to work together to redesign services around the needs of citizens, improving outcomes, reducing duplication and waste and so saving significant sums of public money.

2.22 All these initiatives are welcome and empower local places. But this approach is piecemeal and creates complexity. It is as though the Government is prepared to dip its toe, or even several toes, in the water but is not yet prepared to accept the logic of its position with the confidence it should. We need to go further and faster to achieve an essential rebalancing of central and local power and resources, extending not just to cities, but to local areas right across England.

2.23 The work Sir Terry Leahy and I did in Liverpool in 2011 showed again that when local leaders are brought together, they know better than anyone a city's unique strengths and potential problems²³. Crucially, they know best what needs to be done. When they develop partnerships and collaborate together to solve shared problems the solutions are usually plentiful. These solutions are ones that will not be found in Whitehall. No one in Whitehall can know how to solve the specific challenges facing a particular local area. Separate attempts to solve different local problems will never be as effective as a locally led, joined-up approach.

What is to be done?

2.24 Local places will never be sufficiently empowered to drive the growth we need unless we share the Government's most important lever – funding.

2.25 We need to pass much more of the initiative for deciding how funding is spent from central government to a local level. We need to enable local partnerships to take a holistic view of the challenges they face and develop strategies grounded in the economic reality of their area. This would prove a significant economic and social stimulus over the medium and long term.

2.26 Devolving funding to local leaders will always require a partnership with central government. The redistribution of resources involved, and the proper and unavoidable responsibilities of government, require it. Governments in the end are elected to govern and are accountable for their policies and the use of the taxes they collect. But the initiative and delivery should rest with local leaders.

2.27 To make this new model work central government needs to become much more strategic and much more confident in its actions. It must provide the overarching vision for how best to achieve growth in the UK economy, setting out its national strategy for growth. This is essential. It has already, for example, set ambitious targets for increasing exports. It should be equally clear in its intent across the economy. All parts of government have

²³ *Rebalancing Britain: Policy or Slogan? Liverpool City Region – Building on its strengths: An independent report*, Lord Heseltine and Sir Terry Leahy, 2011 <http://www.bis.gov.uk/assets/biscore/economic-development/docs/r/11-1338-rebalancing-britain-liverpool-city-region>

a role to play in driving economic growth and must act in concert to deliver that vision. I describe the vision I have for central government in Chapter 3. A diagram setting out how I believe the central and local elements should fit together is shown in Annex C, alongside a representation of the current system.

A single funding pot

- 2.28** Until recently when government has allocated funding to local areas – beyond the formula grant for the services local authorities are required to provide – it has done so in penny packets. Parcels of cash attached to specific projects, each with their own particular objectives, timetable and requirements. As I have set out already, there have been individual initiatives giving local communities more influence over how specific funds are disbursed. These are very welcome but again they are not enough.
- 2.29** We need to brigade the separate funding streams which support the building blocks of growth into a single funding pot for local areas. I have produced an indicative list of central budgets that would be more effectively managed by local leaders based on a first examination of the public expenditure accounts. These include significant parts of the skills, infrastructure, employment support, housing, regeneration and business support budgets held by central government. Local leaders would have flexibility to spend the budgets on priorities relevant to local circumstances as agreed with central government.
- 2.30** I estimate that if the Government had been using this approach for the current spending review period the total funding available would have been approximately £49 billion. This is set out in the table below, with a more detailed breakdown of the different funding lines at Annex D. Of course, the exact amount will depend on the levels of public expenditure set in the next spending review.

Table 2.1: Indicative single pot

Funding streams	4 year spending period (£ million) ²⁴
Skills	£17,435
Local infrastructure	£14,821
Employment support	£5,466
Housing	£6,800
Business support services	£2,939
Innovation and commercialisation	£1,611
Single pot total	£49,073

Source: Calculations based on data from government departments

²⁴ All numbers presented to nearest £ million. The total does not equal the sum of the rows due to rounding.

2.31 None of this is new. It is what we did with the Urban Development Corporations, City Challenge. And what we are doing now with the RGF. The departure here would be to apply this model comprehensively across England, and on a far larger scale, so that all our communities can benefit from the opportunity to shape their own economic future. It would transform the way we spend public money in our country. Existing funding commitments mean that the earliest this system can be introduced as a whole is from the next spending review, starting in 2015/16. However, the Government should continue to look for opportunities to devolve funding before then, such as through the City Deals.

2.32 A more comprehensive commitment to devolution will enable an ambitious dismantling of the existing national bureaucracies. This is a significant advantage. The current piecemeal policies require the maintenance of multiple existing structures to administer national funds for local areas still operating under central control.

Recommendation 1: Central government should identify the budgets administered by different departments which support growth. These should be brought together into a single funding pot for local areas, without internal ring fences.

2.33 All my experience confirms that competitive funding is key to unleashing the entrepreneurial spirit in local areas. It injects a surge of excitement and incentivises communities to seek a wider and much more ambitious vision to anything they had thought of before. A healthy rivalry between areas comes into play. It drives collaboration, creativity, commitment and ambition. I therefore believe that the single pot of central government funds for economic development should be made available to local areas on a competitive basis. My experience with the RGF showed that the quality of projects improved round-on-round precisely because of competitive bidding. No one wants to lose, so bidders learn from the successes of the best and the mistakes of the worst. This continually drives up quality and delivers value for every pound. This is in contrast to the usual functional allocation of public money along the lines of formula grants, where recipients know there is always money for them, regardless of what they did with their previous allocation.

2.34 Some will say that a competitive process has drawbacks. It can take longer to get up and running than a formula allocation system. That is a fact. But the partnerships built in that time will pay dividends for decades.

2.35 Others will object to the fact that some areas may lose out. I think that this is important. Most will learn and raise their game quickly. The bidding process – through its assessment of the strengths and weaknesses of different proposals – will reveal where local partners need help from government. I have two arguments. If the bids are of low quality because of inadequate performance by the local partners, then the Government should support them to improve local capability and their bid. But there is a much more likely problem. This arises when the local partners face the challenge of very limited local economic strengths on which to build. A weak bid may reveal such a problem in stark reality.

This is, however, to be welcomed. In exposing the problem it will hasten the urgency to tackle it which may require specific interventions from government.

- 2.36** These issues need to be dealt with as they arise but there is no other mechanism that stimulates the partnership working, ambition and funding leverage generated by competitive bidding.
- 2.37** The Government must also give local areas certainty over their future funding for sufficient periods of time. One of the most frequent complaints I hear from the private sector is that policy changes and political cycles too often result in investment uncertainty. Government policies and funding start and stop, or change their name and criteria, with bewildering frequency. This limits the private sector's ability to act as an effective partner in economic investment. To build for the future we must plan for the long term. For the single pot, this means that funds should be committed to local partners for periods of at least five years at a time. For major investments, specific longer term commitments will be needed once bids are approved.

Recommendation 2: Local partnerships should bid for funds from central government on a competitive basis. Bids should be for a minimum of five years starting from 2015/16.

- 2.38** My analysis at Annex D is only indicative of the amount of money which could be made available to local areas to forge their own economic future. It is for the Government to determine the precise contents of the single pot. There is some funding for economic development I suggest is left out. Central government should retain responsibility for major national infrastructure – the motorway network and mainline rail network, for example, need to remain nationally funded and managed. I have therefore also deliberately left out some funding streams which would need to be divided between national and local spend, such as the money spent by the Highways Agency and Network Rail on transport infrastructure.
- 2.39** I have also left out a number of funding streams intended to provide businesses with access to finance. Some of the Government's current efforts to improve access to finance are a response to the very exceptional issues with the credit markets since 2008. However, where there is a long term market failure, and continuing need for government support for business finance, this could eventually be devolved.

Streamlining EU funding

- 2.40** In addition to central and local government funds, there are currently four streams of EU funding available to communities in England worth £9 billion for the period 2007–2013. These funds are likely to remain a significant source of support for economic development in the medium term. However, the current, separate management arrangements for the funds in England lack any strategic or operational synergies, despite the funds sharing complementary aims and similar regulatory requirements.

- 2.41** For 2014–2020, the funds will be brigaded under a ‘common strategic framework’. The Government should take this opportunity to streamline management arrangements to enhance the combined impact of the funds. They need to strip out unnecessary red tape, reduce cost and risk and enable delivery partners, including businesses, to play a full role. Where the specific objectives of each fund converge – on innovation, SME competitiveness, low carbon developments, community-led initiatives and training – a single offer to the market should be made.
- 2.42** These simplified EU funds should be aligned with the single central funding pot in order to create local investment programmes which integrate EU and non-EU funding and better leverage private finance. Only by doing so will the Government maximise the economic benefit of its own investment. This will require using EU funds in a more sophisticated mix of contracts, loans and grants which better respond to the public spending challenges of the next five to 10 years. The bookkeeping and accountability to Brussels for spending EU funds should be managed centrally. The current complex system for EU funding in England and a new proposed simpler funding model are illustrated in Charts 2.2 and 2.3.

Recommendation 3: Government should streamline its management of EU Common Strategic Framework funds in England, strip out the bureaucracy of multiple programmes and align local allocations from the four funds with the single funding pot.

- 2.43** Local authorities currently invest £11 billion each year in capital projects. This is over and above the funding they receive from central government. Local authorities raise this money partly through borrowing money and realising assets. This additional spending, combined with the single pot and the EU funds, could have an enormous impact on local economic development. Local authorities should consider how these funds can best support the wider plans for local economic development and, in particular, help lever in additional private sector investment.

The role of LEPs

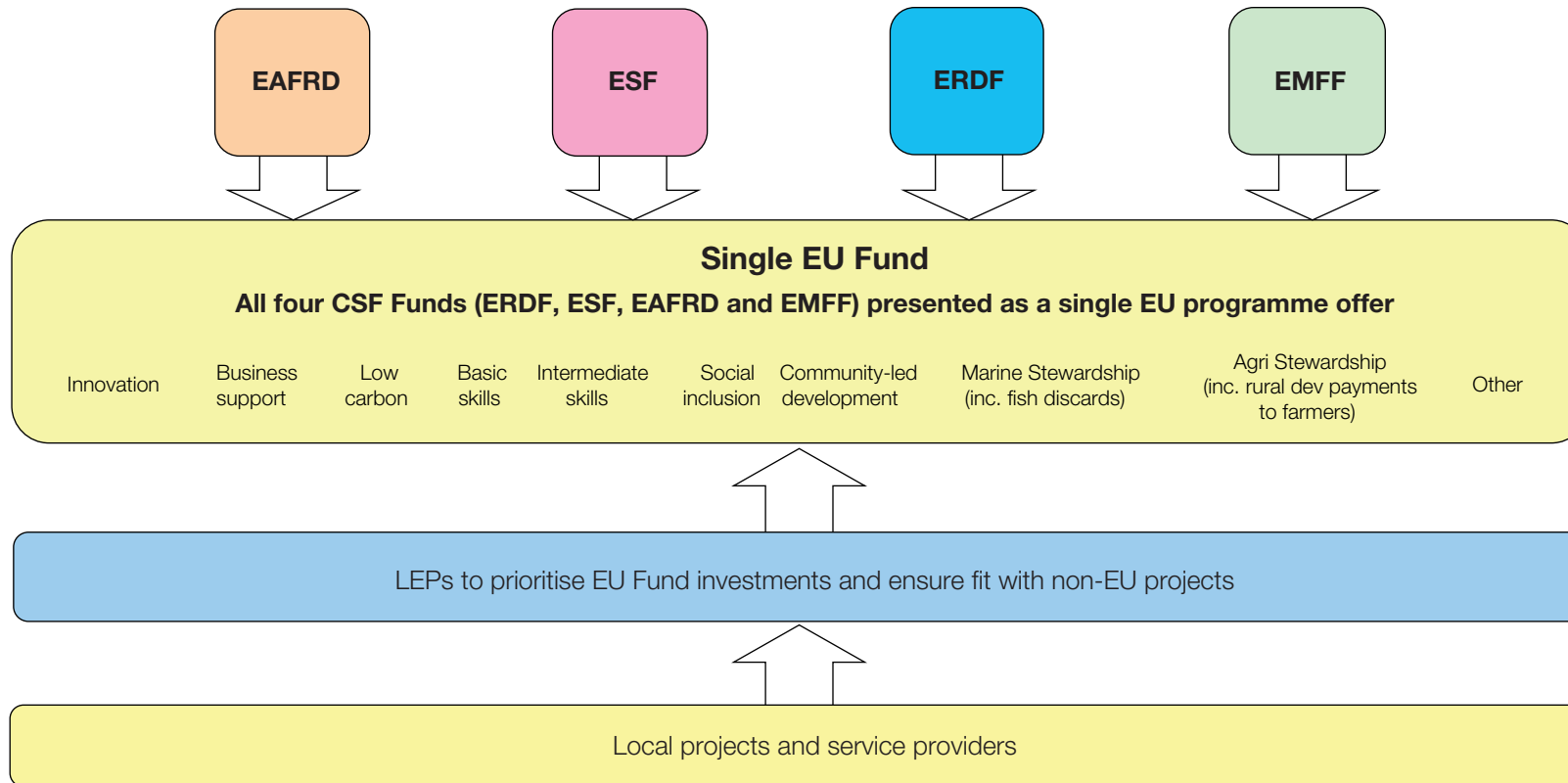
- 2.44** LEPs are the Government’s chosen engine of local growth and there are some early successes that demonstrate their potential. At present LEPs simply do not, though, have the authority or resource to transform their locality in the way our economy needs. This needs to change. LEPs are ideally placed to lead the development of a long term strategy and business plan for their local area. I believe they should develop, with local partners, the bids to secure central government funding for their locality.
- 2.45** In my conversations with LEPs and local authorities I was surprised that not all areas had a robust plan focused on the growth of their local area. Successful businesses plan for the long term, setting out their vision and goals and how they will compete. A plan is necessary to achieve any vision. It brings discipline and focus and helps ensure that there is the widest possible buy in to the final objective.

Chart 2.2: Common strategic framework funds – current programmes 2007–2013 (England)

Description of Fund	European Regional Development Fund – €3.3bn										European Social Fund – €3.1bn	European Agricultural Fund for Rural Development – €3.2bn	European Fisheries Fund – €48m
<p>10 regional programmes – each has between one and four priority axes, many following similar themes but often with a slightly different emphasis. Separate calls for bids for funding on sub-priorities – timetable determined regionally. Funding must be used strictly within region where allocated. CLG is the Managing Authority (MA). BIS is the Managing Authority (MA). BIS has legislative and policy oversight and reports on performance to European Commission.</p>											<p>One national programme Two priority axes DWP is the MA BIS has the legislative lead and reports to European Commission</p>	<p>One national programme Four priority axes Defra is UK MA Defra has legislative and policy lead and reports to European Commission</p>	<p>One national programme Four priority axes Marine Management Authority is UK MA Defra has legislative and policy lead and reports to European Commission</p>
National Programmes											ESF England and Gibraltar	Rural Development Programme for England	European Fisheries Fund (England)
Regional Programmes	North West	North East	Yorkshire & the Humber	West Midlands	East Midlands	East of England	London	South East	South West Competitiveness	Cornwall and Isles of Scilly			
Priority axes eligible for funding under the programme	<ul style="list-style-type: none"> <li style="background-color: #e6f2ff; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Exploiting innovation and knowledge <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Stimulating enterprise and supporting growth <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Creating conditions for sustainable growth <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Growing and accessing employment 	<ul style="list-style-type: none"> <li style="background-color: #e6f2ff; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Enhancing and exploiting innovation <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Business growth and enterprise 	<ul style="list-style-type: none"> <li style="background-color: #e6f2ff; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Promoting innovation and R&D <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Supporting and stimulating successful enterprise <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Sustainable communities <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Economic infra-structure for a competitive community 	<ul style="list-style-type: none"> <li style="background-color: #e6f2ff; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Promoting innovation and R&D <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Stimulating enterprise development <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Achieving sustainable development <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Developing inter-regional activity 	<ul style="list-style-type: none"> <li style="background-color: #e6f2ff; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Business innovation and research promoting co-efficiency <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Sustainable economic and enterprise activity in disadvantaged communities 	<ul style="list-style-type: none"> <li style="background-color: #e6f2ff; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Promoting innovation and knowledge transfer <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Stimulating enterprise and supporting successful business <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Ensuring sustainable development, production and consumption 	<ul style="list-style-type: none"> <li style="background-color: #e6f2ff; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Business innovation and research promoting co-efficiency <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Sustainable places for business <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Access to new markets and access to finance 	<ul style="list-style-type: none"> <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Promoting sustainable production and consumption 	<ul style="list-style-type: none"> <li style="background-color: #e6f2ff; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Innovation and knowledge <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Enterprise and growth <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Urban enterprise 	<ul style="list-style-type: none"> <li style="background-color: #e6f2ff; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Innovation and research development <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Enterprise and development <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Transformation and infrastructure <li style="background-color: #fff2cc; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Unlocking the economic potential of place 	<ul style="list-style-type: none"> <li style="background-color: #f080f0; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Tackling barriers to employment <li style="background-color: #f080f0; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Improving skills of local workforce 	<ul style="list-style-type: none"> <li style="background-color: #ffcc99; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Improving the competitiveness of the agricultural and forestry sector <li style="background-color: #ffcc99; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Improving the environment and the countryside <li style="background-color: #ffcc99; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Quality of life in rural areas/ diversification of rural economy <li style="background-color: #ffcc99; border: 1px solid black; padding: 2px; margin-bottom: 5px;">LEADER (community-led projects) 	<ul style="list-style-type: none"> <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Adjustment of fishing fleet <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Aquaculture, processing and marketing <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Measures of common interest <li style="background-color: #c1e1c1; border: 1px solid black; padding: 2px; margin-bottom: 5px;">Sustainable development of fisheries areas

Key to ERDF priorities: Innovation and R&D Sustainable development Support for enterprise Miscellaneous

Chart 2.3: Future EU common strategic framework funds 2014-2020 (England) – a potential streamlined option



- 1. Integrates EU and UK funds:** hiding the wiring to delivery partners
- 2. Promotes local leadership:** strong role for LEPs
- 3. Increases flexibility for projects:** no geographic restrictions and opportunities to draw from all four EU funds
- 4. Cuts red tape and admin cost:** consolidates administration and removes geographic barriers
- 5. Strengthens risk management:** annualised error rates, performance and spending targets can be managed at national level, minimising exposure to fines and budget losses.

- 2.46** That is why all functional economic market areas need a strategy and thorough business plan in place that clearly sets out a vision for growth. Liverpool, Manchester and Newcastle upon Tyne are places that either have or are in the process of developing such documents.
- 2.47** This plan should include an analysis of the strengths and weaknesses and barriers to growth of the area. It should include an investment plan that can be used to bid for central government funds and take account of other sources of finance. This plan would be the road map for how the local area could improve its performance. It would need to be developed in conjunction with local stakeholders, businesses and their representatives, education institutions and local people. Local areas will need to answer difficult questions: what are our areas of competitive advantage, what are our structural weaknesses, what skills gaps do we have and how can we fill them, how do we get the long term unemployed back to work?

Recommendation 4: Taking full account of the Government’s national growth strategy, all LEPs, in collaboration with local stakeholders, should lead the development of a long term strategy and business plan for their area that will be used to bid for economic growth funds from central government.

- 2.48** The Government will need to set out the requirements that LEPs must meet in their bids to secure funding. It should consult LEPs, local authorities and the business community in doing so. It is important that this framework is focused on high level outcomes and does not become detailed and prescriptive. This would rein in the creativity of local areas and undermine the benefits of local empowerment. However, there will be some essential criteria which have to be met for government to devolve such significant funding. For example, the LEPs would need to set out:
- > how their bid contributes to national growth priorities
 - > how their bid would leverage the funding, creativity and support of local partners in the public and private sectors – this could include deploying existing local authority funding streams in support of the LEP plan
 - > how local people and businesses had been consulted, what their views were and how they would be engaged in delivering the plan
 - > robust but simple governance arrangements, working in partnership with the relevant local authorities, and how those local partners would be accountable to their locality for delivery of the plan
 - > how they will learn from what they do, and share that learning with other LEPs.
- 2.49** The Government would also need to set out its evaluation framework and subsequent arrangements to monitor the impact of the funding provided. An example of a possible bidding framework is attached at Annex E.

- 2.50** Once a LEP has been allocated funds²⁵ it should be free to implement its strategy, accountable to its local community but free from central government diktat. Events are unpredictable. There will be a constant need for reappraisal, new initiative, a search for new projects to replace ones that fail to get off the ground or where change is needed. That is how the private sector works. LEPs must be enabled to respond to economic shocks or opportunities in their areas. Criticism should be levelled not at people who tried to achieve a project which proved too ambitious. Criticism should be aimed at people who do not try at all.
- 2.51** I am confident that we will be surprised by the quality of the plans that local areas can develop with the promise of new powers and resources. In the course of the review I asked Birmingham and Manchester to give their views.

What the new model could mean for Greater Birmingham and Solihull LEP

Our Greater Birmingham and Solihull LEP has fused political and business leadership and over the past two years demonstrated our ability and vision to change the economic fortunes of our city region. We have created the largest city-centre Enterprise Zone in the UK, and a wide ranging City Deal which will create over 50,000 new and sustainable jobs.

With a single settlement and greater devolution of powers and funding we could do even more. For example:

Transport and Infrastructure: We could maximise the impact of major national investments like High Speed 2, link them to our transport network and deliver major schemes faster by removing lengthy bidding and approval processes. If these powers had been in place 10, or even five years ago, significant transport projects which are now only just being built such as New Street Gateway would be operational, linked into a coordinated transport network and providing a £2 billion benefit to the region.

Housing: We could overcome the challenges of housing growth by developing further 'build now, pay later models' for public sector land and providing the necessary supporting infrastructure – meeting demanding housing growth targets, and building new jobs and businesses through the supply chain.

Growing leading sectors: We could build on existing assets (particularly around Life Sciences and Automotive) with a complete package (skills, business support, infrastructure, Foreign Direct Investment) to give the UK internationally competitive sector strength, creating approximately 73,000 jobs in our local supply chain.

²⁵ Each LEP should nominate a lead local authority to hold and administer the allocated funds on its behalf. This provides the simplest means to ensure appropriate and effective management of public funds.

Greater Manchester

Greater Manchester has established the first combined authority²⁶ which provides strong, accountable leadership and a platform for devolution to the city region. Through this and the city deal agreed in March 2012 Greater Manchester has gained new powers and responsibilities that allow economic growth to be driven locally for the benefit not just of the Greater Manchester economy but for the UK as a whole. This includes responsibility for economic development, transport and housing and bespoke arrangements to support economic growth including the innovative ‘earn back’ model which allows Greater Manchester to capture a proportion of the economic benefits of local infrastructure investment to reinvest in growth enhancing projects.

A second wave of devolution from central government should build on this and allow Greater Manchester to go much further, providing the conditions necessary to meet our potential and create over 75,000 jobs over the next five years. It should increase local decision making, driving growth in key sectors, and flexibility for greater integration of business support, trade and investment. However, the key priority will be to increase productivity and, through the actions of the Community Budget pilot, provide a platform for public sector reform that will reduce dependency on high cost public services. At the same time, this should retain accountability to ministers for delivery of national priorities. Greater local responsibility for skills and work would significantly strengthen the effectiveness of labour markets. New delivery and investment models at Greater Manchester level will incentivise decision making across public service boundaries. This is essential to underpin economic growth at the same time as meeting the financial challenges faced across the public sector.

- 2.52** While LEPs would not be able to access this new funding model until 2015, I would not expect any to sit on their laurels in the meantime. As well as the serious business of developing their local strategic plans, all LEPs should continue to work from today to expand their role in economic development. In particular they should consider what other funds they can deploy before 2015.

Building the capability of LEPs

- 2.53** With a new enhanced role for LEPs, it is important they have the skills and capabilities to deliver. So far, they have had to rely largely on their own resources. I welcome the Government’s recent decision to provide core funding to ensure all LEPs are sustainable and able to focus on the fundamental task of generating local economic growth. However, this is not in itself enough. LEPs will need resources to develop their plans and to prepare

²⁶ A combined authority is designed for groups of relevant local authorities that wish to work closely together to deliver improvements in economic development, regeneration and transport across a sub-region.

for the tasks of implementation – procurement, contract management and project management for a start. Some of these resources will be provided by partners in the LEP in the form of staff time or activity, but additional seed funding will be required.

- 2.54** LEPs should therefore be given additional funding, specifically to develop their new strategic plans. This must be used to hire professional private sector planners as part of a deliberate attempt to spread best practice, engage private sector expertise and avoid LEPs being entirely dependent on the already stretched planning departments of their local authorities. I instituted such arrangements for the rebuilding of Manchester city centre following the 1996 bombing. They worked well.

Recommendation 5: The Government should allocate LEPs up to £250,000 of new public funding, resourced through departmental efficiency savings and underspends, in each of years 2013/14 and 2014/15 specifically to devise their local economic strategies, and create the foundations for their implementation.

- 2.55** Some will say that I am recommending the creation of 39 new bureaucracies. The facts are different. This government has established the LEP concept. I strongly support the initiative. My only involvement is to improve its effectiveness. Many existing and complex bureaucracies in central and local government could be reduced and streamlined to focus more clearly on the Government's growth agenda. While it is inevitable that LEPs will need to grow in order to take on the leading role I have proposed, they will remain entirely autonomous local partnerships, democratically accountable through their local authority members. I am confident that the sum total of their overheads will be significantly less than the bureaucracies which currently serve the plethora of existing functional funding systems.

Sheffield City region

The Sheffield City Region LEP has been instrumental in unlocking growth in the *Chesterfield Waterside* development.

Local public and private sector partners were successful in leveraging approximately £18 million of additional funds on the back of a £2.4 million allocation from the Growing Places Fund.

The funding will be used to unlock the first phase of a residential development through the construction of a new canal arm and lock infrastructure, and improved road bridge access to the site. When fully built out, the Chesterfield Waterside development is expected to provide 1,500 housing units, 30,000 square metres of commercial office space, and a retail and leisure offer centred around a new canal basin. Overall, the development will result in 2,200 jobs being created.

Cumbria Local Enterprise Partnership

Cumbria LEP, working with partners, primarily Cumbria Chamber of Commerce and Cumbria County Council, has put together a coherent package of support centred on its Rural Growth Network (RGN) pilot, with total funding of around £20 million for rural growth and businesses countywide. This includes EU and RGF funds plus contributions from partners including the chamber, Cumbria Council, Britain’s Energy Coast, enterprise agencies and local universities.

The RGN will focus on food and drink, digital and creative, agri-business and adventure and country sports businesses. It will also provide support for social and women-led enterprises through 11 physical hubs, six key employment sites and a range of networking and business support. It aims to create around 480 business start-ups and 900 jobs. RGN activities will link with an EU funded start-up scheme and Growth Hub that will provide a web portal and phone service, plus physical and virtual business support activities that link businesses into the wider range of support. The RGF programme will provide grants to specialist manufacturers, exporters and SMEs and deliver a range of specialist low carbon support that will also benefit rural businesses. Cumbria is working closely with other LEPs and will share learning from its RGN and Growth Hub.

Cornwall and Isles of Scilly Local Enterprise Partnership: Regional Growth Fund bid

The Cornwall and Isles of Scilly LEP secured £13 million from the second round of the RGF. The LEP will leverage additional funding to create a £43 million programme which will directly create or safeguard 3,200 jobs and indirectly create a further 2,100 jobs.

The funding will be allocated in two ways. First, competitively, by providing businesses and social enterprises with capital grants and investments to grasp the opportunities presented by superfast broadband. Second, through funding infrastructure projects in the marine, mineral, renewable energy and aerospace industries which will unlock private sector investment.

Matching LEPs to functional economic market areas

2.56 Matching LEPs to functional economic market areas is vital as it ensures that the full range of barriers to growth in a local economy is considered together. It ensures that each LEP is in the best position to identify and align local action to support growth.

2.57 The boundaries of LEPs were proposed by the partnerships themselves. Many reflect the geography of local functional economic market areas, but there are anomalies. This is not

an exact science – there will always be debates about precisely where the lines should be drawn. As LEPs are so central to the future economic growth of this country they should be asked to reassess and confirm that their boundaries, as far as is practicable, do align with functional economic market areas.

- 2.58** At present some LEPs overlap. These overlaps need to be removed so that there is a single partnership with clear ownership for economic development in every part of England. In the same way that neighbouring local authorities do not overlap, but come together on common issues, LEPs need to evolve to work to the same principle. This must be achieved as a matter of urgency to ensure that communities served by LEPs whose boundaries overlap are able to see a single vision and a compelling plan for their area.

Recommendation 6: The Government should invite LEPs to review their boundaries within a three month period to ensure they have a good match with their functional economic market area and that they do not overlap.

Composition of LEP boards

- 2.59** The composition of LEP boards is an important condition for their success. LEPs must be led effectively and represent the breadth of local leadership that will drive economic growth. From what I have seen, the balance of interests on each LEP's board is usually effective. There is one area however that seems to me to be worth adjusting. Public sector employees are already heavily represented through the local authority members. What is missing is the experience of those from the shop floor of industry.

Recommendation 7: In light of the new role and vision for LEPs, each LEP should ensure that their board has the necessary skills and expertise to deliver their expanded functions and pay particular attention to the representation of employees from both private and public sector.

- 2.60** I set out a timetable for all the work that needs to be done with LEPs and other partners to introduce a competitive funding pot in Chapter 7.

Lack of central government interest in place and localities

- 2.61** To be effective, the voice of LEPs will need to be heard in central government to cut through process and champion their ambitions, especially when departmental policies cut across one another. At the same time there is a danger that central government will maintain its functional preoccupation and LEPs their place based policies, each hindering the other.

Local growth teams

- 2.62** When this government came to power it abolished the Regional Development Agencies (RDAs). This was understandable. They were based around administrative, not economic

boundaries and were, to all intents and purposes, creatures of central government. Localities were invited to form collaborations of private and public sector partners in the form of LEPs. At the same time, the Government Offices which were created to provide a unified local presence for stakeholders to work with around the country were closed.

- 2.63** Across the country there are now disparate teams of civil servants taking forward roles and functions important to central departments such as Transport, BIS, CLG, DEFRA and UK Trade and Investment. In other words the dispersed arrangements in place in the early 1990s have inadvertently been resurrected. In many cases where offices are shared, informal arrangements are continuing to provide some coordination. While this is welcome, collaboration should not be ad hoc. All public servants based across the country and working to deliver common goals should be actively collaborating with one another, and no more so than where such collaboration influences economic growth.
- 2.64** This leads to the conclusion that we should bring together civil servants from different departments whose work impacts on the economy into Local Growth Teams so they can work seamlessly together, closer to the people and agencies affected by their work. They should facilitate both economic development matters that straddle LEP boundaries and partnerships around and between functional economic market areas. They should play an important role in joining up local and central government and act as the eyes and ears of Whitehall to help central government consider local place as it develops policy, as opposed to just retaining the present functional approach.
- 2.65** As the conduit for a two-way dialogue, the Local Growth Teams will be instrumental in ensuring that LEPs produce the best strategies they can, avoiding pointless duplication in LEP strategies – for example 15 areas all bidding to be the national centre of excellence for life sciences – and in ensuring that government’s national objectives are met by the aggregation of the individual LEP strategies.
- 2.66** On the basis of past experience it would seem that there would need to be in the order of six to seven Local Growth Teams, each working to support a different cluster of LEPs.
- 2.67** It is also important that we reduce waste and make the most of the hidden resource in the present dispersed array of land holdings in the public estate. Establishing Local Growth Teams fits well with the essential rationalisation of the government estate and modernisation of the civil service being driven by the Minister for the Cabinet Office. As part of this rationalisation, the Cabinet Office will have an important role in considering the most effective spread of Local Growth Teams across England.

Recommendation 8: At the earliest opportunity civil servants based across the country should be brigaded into Local Growth Teams, structured around clusters of LEPs, primarily tasked with joining up government and local partners in the areas of their responsibilities to facilitate, identify and realise economic opportunities.

2.68 Ministers need to be encouraged to think outside the functional responsibilities of their departments. Regional ministers have been tried before, but were always trumped by their colleagues with control of the functional levers of government. After the riots in Liverpool I visited the city most weeks for 18 months – the benefit to my departmental responsibilities was profound. It would greatly improve ministerial understanding of the policies of place if each cabinet minister were associated with two LEPs. They would be expected to visit these LEPs at least every two months.

2.69 Permanent secretaries should be associated with particular LEPs in a similar way to help ensure that officials across Whitehall take into account the holistic impact of their departmental policies on particular places.

Recommendation 9: Ministers and permanent secretaries should be associated with individual LEPs, not to advocate individual plans but to add an understanding of place to the existing culture of function.

2.70 Local engagement from a wide range of partners such as business, chambers of commerce, educational institutions and local authorities will result in thorough scrutiny of each LEP's activities. That alongside the role of Local Growth Teams makes it, in my view, unlikely that a LEP would become so ineffective as to not be able to fulfil its role. However, should this happen the power to withdraw public funding and responsibility from the LEP and recognise a successor should rest with government.

Effective and empowered local authorities

2.71 While the new funding model and the requirement for LEPs to produce a strategic plan should help to focus attention on creating growth, they will need effective and empowered local authority partners. There are additional steps that need to be taken to encourage local authorities to have sufficient regard to economic development and address the bureaucratic inefficiencies inherent in the English system of local government. These are particularly difficult to defend at a time when the public finances are facing such considerable constraint. I do not pretend that any of what follows will be easy.

Incentivising economic development

2.72 I have described how, over time, local authorities have come to focus on social provision at the expense of economic development. Many of these functions are vital – from safeguarding vulnerable children and adult social care, to trading standards and waste management – and are therefore underpinned by legal duties. There is no legal duty with the sole purpose of focusing local authority action on economic development. Where there are requirements around economic development they are usually a consequence of a broader policy requirement and they do not align. This simply reinforces a belief that for local authorities economic development is secondary to their social functions. The consequences can be insufficient attention given to local economic development,

differences in interpretation of the role of local authorities, and a failure to protect economic development from being the first activity to be axed by authorities when finances are tight.

2.73 The Government should therefore send a clear signal to all local authorities to embrace the good practice of their leading peers by providing them with a new overarching legal duty to have regard to economic development across all their activities and in the exercise of all their functions.

2.74 In addition, the boundaries of local government are in most cases the product of history. They often have little relation to current functional economic market areas. In order to play their part fully in economic development, local authorities need to collaborate together. This collaboration should be aligned with the local functional economic market area and therefore also aligned to LEP boundaries. This, taken together with the incentives the Government has put in place and those I propose, should ensure all English local authorities are more active in exploring opportunities for greater collaboration, joining forces within functional economic market areas to pursue growth, and sharing responsibilities and administrative services wherever appropriate.

Recommendation 10: Local authorities should have a new overarching legal duty to have regard to economic development in the exercise of all their activities and functions. Where local authorities share a functional economic market area they should be required to collaborate on economic development.

Bureaucratic inefficiency and the case for unitary authorities

2.75 The multi-tiered nature of the English local government system makes it even more difficult to exploit economic opportunities fully. The duplication and inefficiencies, blurred lines of accountability and competing local leadership constrain local government from functioning effectively.

2.76 Businesses prefer to deal with one local authority instead of speaking to multiple authorities, where each has a slightly different focus, set of priorities and objectives. Speaking to one authority would be simpler and lead to faster decisions. This is important if we are to identify and exploit economic opportunities.

2.77 Redcliffe-Maud recognised this in the 1960s when he recommended a completely new structure for local government. The boundaries of LEPs, based around functional economic market areas, are remarkably similar to his proposals (see Charts 2.4 and 2.5). I fully support Redcliffe-Maud’s approach and believe we need to adopt the concept of unitary authorities across more of England. The new LEP architecture provides an excellent starting point. The current financial squeeze on local budgets will in any case drive rationalisation.

- 2.78** Unitary authorities run local services effectively and at considerably lower cost. They provide greater clarity and accountability about where responsibilities lie for delivery of local services. They avoid duplication and coordination issues that can arise between different local authority functions. They facilitate faster and more robust decision making and avoid the unnecessary administrative expense associated with running a two-tier system.
- 2.79** In the 1990s we created unitary authorities in Wales and Scotland. When I visited Scotland and met with representatives from the Convention of Scottish Local Authorities (COSLA), I asked them if they had any views on the benefits of unitary authorities versus a two-tier system. They did not entertain the idea for a moment. Few of them were around when the two-tier system was abolished sixteen years ago, and none of them could imagine why anyone would want to go back.
- 2.80** I heard a similar story in Wales where they also long ago recognised the efficiency gains and benefits that can be achieved through a single tier approach. In 1996 its former city and county councils were merged to create 22 unitary authorities to reduce bureaucracy, prompt more streamlined and efficient decision making and focus more resources on front line services.
- 2.81** Changing to a unitary model of local government will not be easy. It will naturally be uncomfortable for those involved, it may be disruptive in the short term and it will take time. But it would be a mistake not to persevere. The costs of the two-tier system are simply unsustainable. The advantages in increasing effectiveness and freeing resource for the benefit of communities will outweigh the pain.
- 2.82** Local authorities which have made the transition to unitaries have found that while there can be significant initial costs, these are recovered in as little as three years, with ongoing savings thereafter. Cornwall is a case in point. In 2009 it made the transition to a unitary council by reorganising seven councils into a single unit. The initial cost was £39.5 million, but the reorganisation is now delivering ongoing efficiency savings of £15.5 million a year. It has also enabled the council to deliver significant other savings and capital investments in the medium term that, although not directly attributable to moving to a single authority, would not have been deliverable to the same scale had Cornwall retained the two-tier structure.
- 2.83** The transitional costs of creating the unitary Wiltshire Council were £18 million. This compares to a saving of a total £68 million between 2009 and 2013. Back office costs now only comprise 9% of Wiltshire Council's budget as opposed to 19% for its predecessor bodies. The new authority has achieved procurement savings of £36 million through increased buying power and stronger market position. Wiltshire Council has found that customers find accessing its services considerably easier with much less confusion about who is responsible for what. The council is also now in a much stronger position to support economic growth and improve the future prospects of residents and businesses.

Chart 2.4: Map of government areas proposed by Redcliffe-Maud

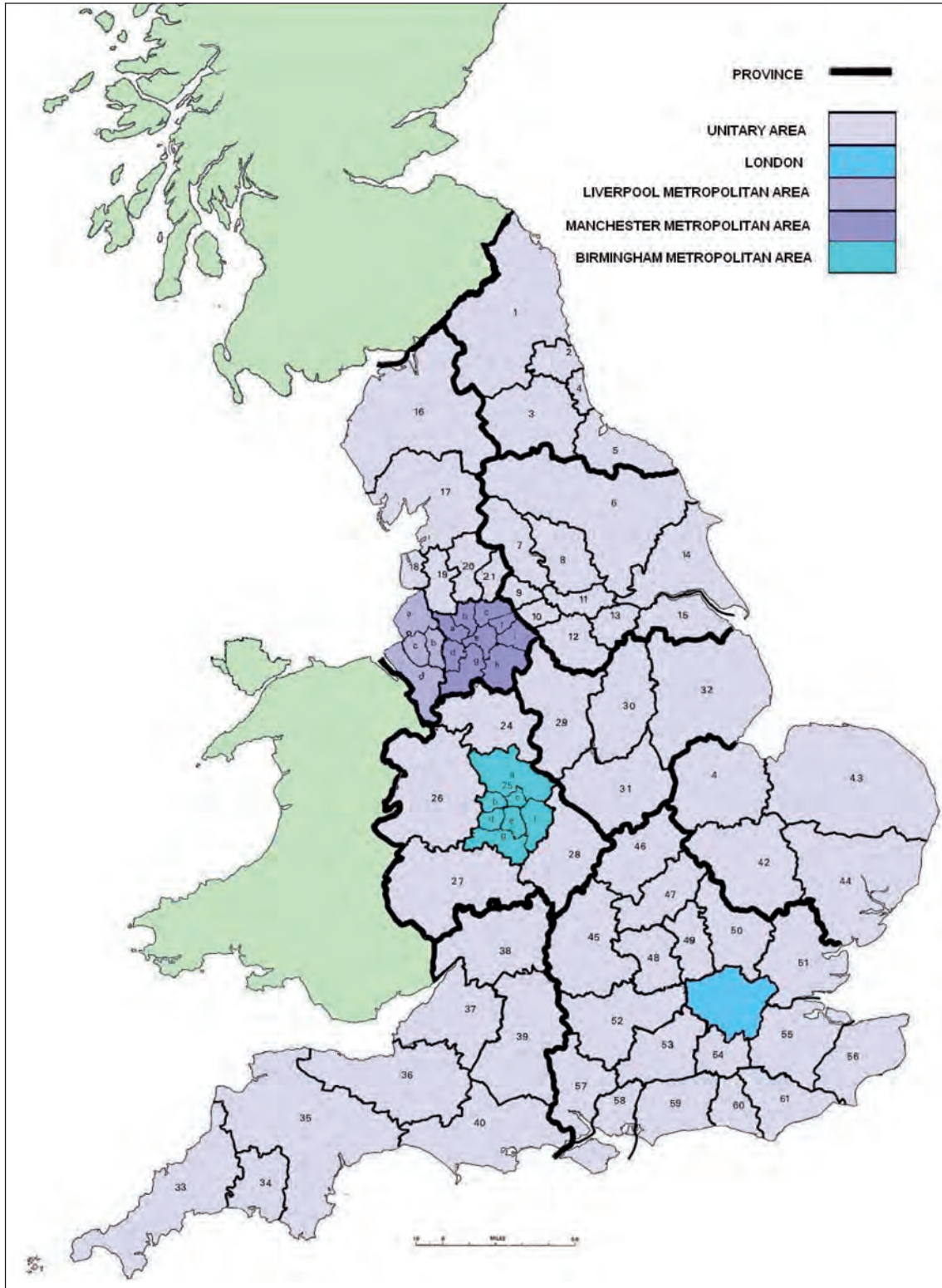
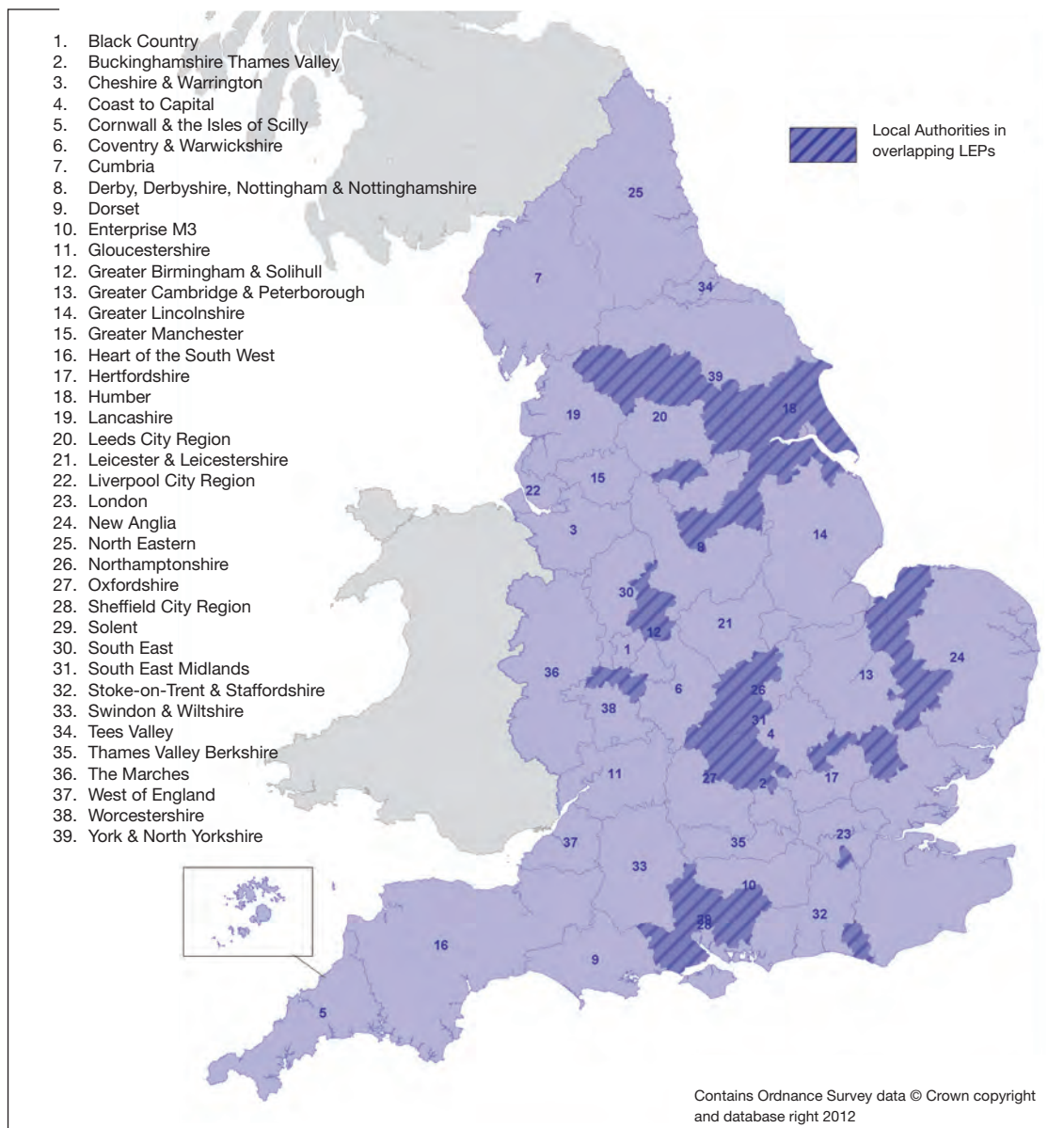


Chart 2.5: Map of LEP geographical boundaries



Recommendation 11: All two-tier English local authorities outside London should pursue a path towards unitary status. The Government should encourage this and work with authorities to clarify the process and enable it to happen.

2.84 In London a single conurbation authority exists although the London boroughs remain powerful in their own right. In the conurbations outside London it would make sense to follow the lead set by Manchester in establishing a combined authority in 2011. Leeds, Sheffield and Tyneside plan to follow suit. Formal collaborations between local authorities across functional economic market areas on matters covering economic development, regeneration and transport should raise the capacity of the areas to drive growth.

- 2.85** When central government is asked to consider a formal collaboration, whether to become a unitary or form a combined authority, it should be important that such collaborations align with the boundary of the relevant LEP – and therefore serve a functional economic geography.

Recommendation 12: Proposals for formal collaboration between local authorities that reinforce the standing of the LEP and enhance the partnership with the private sector across a functional economic market area, should be encouraged and prioritised for government approval. All proposals to move to unitary or combined authority models should be scrutinised by the Prime Minister’s Growth Council (see Chapter 3).

- 2.86** Much of the legislation governing local authorities was conceived before LEPs were established, and before functional economic market areas became the dominant paradigm in local growth policy. This means that some legislation now actually acts as a barrier to collaboration. All authorities should have the option of coming together within a LEP area whether to form a new unitary authority or a combined authority. The legislative framework, and supporting process, should be amended to enable this to happen. The Government should act urgently to address these constraints.

- 2.87** Two years ago the new Coalition acted decisively and rapidly to begin to put the public sector finances on a stable footing. It called an immediate halt to those authorities exploring unitary status to avoid the short term costs of transition. The Local Government Act 2010 which enacted this policy is now to all intents and purposes redundant. In keeping with the Government’s deregulation agenda, and to avoid future uncertainty, when parliamentary time allows the Act should be repealed.

Recommendation 13: The Government should remove all legislative barriers that are preventing local authorities from collaborating within functional economic market areas, including moving to a unitary status.

Local election cycles

- 2.88** The councils that show the greatest leadership are not just those that have a strong leader, but those where all the elected councillors have the time and opportunity to work together to deliver for their communities. Councillors are elected for four year terms, under a variety of electoral cycles that differ across authorities.

Local election cycles

Methods of holding elections to local councils can be:

- > by whole council (all councillors are elected at the same time once every four years)
- > by thirds (at each election a third of the councillors are elected. Elections are held every year except in the year when the county council election is held)
- > by halves (at each election half of the councillors are elected. Elections are held every two years, and not in the year when the county council election is held).

2.89 Each of the electoral cycles has different strengths in providing democratic accountability. However, the cycles whereby a proportion of the leadership team change on an annual basis make anything but short term decision making difficult. This, in my view, is damaging for all forms of local authority services but particularly for economic development with the long lead times to bring new infrastructure from concept to fruition. Those councils which hold one election every four years appear to be better placed to take strategic and longer term decisions to the benefit of economic growth, and without incurring the administrative costs associated with running annual elections and managing change. We should adopt a common electoral cycle whereby every council member is elected at the same time every four years.

Recommendation 14: Local authority council members should be elected using the same electoral cycle across England where the whole council is elected at the same time every four years.

Mayors and the importance of leadership

2.90 Finally, I have always believed that leadership is the key to success in any field. Strong leadership is usually part of the solution to complex problems. It is particularly so to deliver a vision and effect positive change – and no more so than in overcoming the barriers to local growth.

2.91 London already has such a leader, Liverpool and Leicester now too. These cities are the pioneers from which we should learn.

London Mayor

The Office of the Mayor was established by the Greater London Authority (GLA) Act 1999 as part of a wider devolution movement that included Scotland, Wales and Northern Ireland. Over time the powers of the Mayor have been extended. The Office has spending powers with regard to housing and regeneration. The Mayor is also now able to establish mayoral development corporations – the London Legacy Development Corporation being the only one to date – which have strong planning powers. The GLA Group’s gross expenditure budget for 2012/13 is £14.5 billion.

The Mayor has had a big impact on London. London’s congestion charge zone, the decision to build Crossrail, ‘Boris Bikes’ and the successful Olympic and Paralympic Games would not have happened without the leadership and personality of successive mayors.

- 2.92** Earlier this year 10 mayoral referendums took place across England. Most voted against, but Bristol voted in favour and will now be able to elect a mayor who can strengthen local governance, champion issues important to the local community and represent the city on matters of wider importance to the UK. Four of England’s major cities will therefore be mayoralties. In addition there are now 16 unitary authorities with the same pattern of leadership.
- 2.93** I was disappointed that more cities did not choose to opt for a mayor. It confirmed my fear that relatively few would vote and that party loyalties would determine the outcomes. I believe this issue needs to be revisited to give our cities the influence and leadership commonly found in similar economies.
- 2.94** We also need to strengthen the legislation that underpins combined and other authorities that want to collaborate to ensure that local people can choose whether to elect a mayor. They should also be able to do so for wider city conurbations if they so wish. At present, legislation does not provide for conurbation mayors. It is also interesting to note Sir Peter Soulsby was elected Mayor of Leicester and Joe Anderson Mayor of Liverpool, without a referendum, because the local authorities decided that this would make their governance more effective. The Government at this stage should hold urgent consultation and, where broad local support exists, act to facilitate such developments without a referendum.

Recommendation 15: Legislation should be passed to enable combined local authorities, and other combinations of authorities, that wish to elect a conurbation mayor to do so.

NO STONE UNTURNED in pursuit of
GROWTH

Chapter 3:

Whitehall - a confident, strategic centre of government

- 3.1** Most decisions made by government and the wider public sector have some impact on the ability of businesses to create wealth. Government action can be a significant force for good, but it can equally have a negative effect. From taxation to welfare payments, education policy to the research base, procurement to infrastructure, the Government should make the most effective use of all the levers at its disposal to promote growth and improve performance. I say more about specific levers in Chapter 4.
- 3.2** Let me start with a few numbers on the scale of central government. The 17 main government departments currently employ over 260,000 people and there are at least a further 190,000 people employed in the various agencies and non-departmental public bodies (NDPBs) sponsored by departments.

Table 3.1: Central government headcount (by department)

Government departments	Number of staff 2012 Q2 headcount
Department for Business, Innovation and Skills	3,150
Cabinet Office	1,840
Department for Communities and Local Government	1,750
Department for Culture, Media and Sport	460
Ministry of Defence	54,020
Department for Education	2,750
Department of Energy and Climate Change	1,340
Department for Environment, Food and Rural Affairs	2,140
Foreign and Commonwealth Office	6,510
Department of Health	2,350
HM Revenue and Customs	74,200
Home Office	10,710
Department for International Development	1,740
Ministry of Justice	4,450
Department for Transport	1,680
Her Majesty's Treasury	1,180
Department for Work and Pensions	98,540
Total	268,810

Source: ONS, *Public Sector Employment Statistical Bulletin*, (Q2 2012)

3.3 In 2011/12, the public sector oversaw £694.6 billion of public expenditure, amounting to 43.6% of GDP.

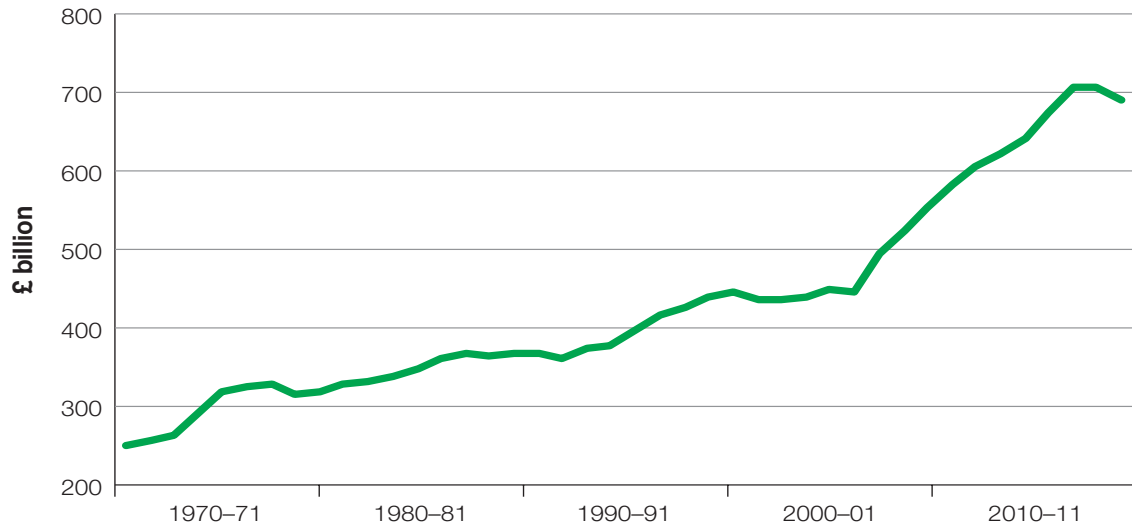
Table 3.2: Public sector expenditure on services by function and as a per cent of GDP 2011–12

	2011/12 outturn	
	% of GDP	Real terms (£bn)
1. General public services	4.5	69.4
<i>of which:</i>		
<i>public and common services</i>	0.8	12.7
<i>international services</i>	0.6	9.1
<i>public sector debt interest</i>	3.1	47.6
2. Defence	2.6	39.1
3. Public order and safety	2.1	32.3
4. Economic affairs	2.2	34.9
<i>of which:</i>		
<i>enterprise and economic development⁽¹⁾</i>	0.2	3.7
<i>science and technology</i>	0.2	3.6
<i>employment policies</i>	0.1	1.8
<i>agriculture, fisheries and forestry</i>	0.4	5.6
<i>transport</i>	1.3	20.3
5. Environment protection	0.7	11.2
6. Housing and community amenities	0.7	10.3
7. Health	7.9	121.3
8. Recreation, culture and religion	0.9	13.2
9. Education	6.0	91.6
10. Social protection	15.9	242.3
EU transactions	0.1	1.2
Public sector expenditure on services	43.6	666.8
Accounting adjustments	1.8	28.1
Total managed expenditure⁽²⁾	45.4	694.9
<small>(1) Transactions from 2008-09 onwards have been affected by financial sector interventions</small>		
<small>(2) Excludes the temporary effects of banks being classified to the public sector</small>		

Source: HM Treasury Public Expenditure Statistical Analysis, July 2012

3.4 Total managed expenditure has risen significantly in real terms over the past four decades.

Chart 3.1: Total managed expenditure (£ billion at 2010/11 prices)



Source: Calculations based on ONS/HMT public finances databank, September 2012, sheet B3

Table 3.3: Public expenditure by decade

Financial years	Total managed expenditure (£bn at 2010/11 prices)
1970/71 to 1979/80	2,991.4
1980/81 to 1989/90	3,580.0
1990/91 to 1999/00	4,257.5
2000/01 to 2009/10	5,845.5

Source: ONS/HMT – see Chart 3.1

3.5 By any standard, central government’s effect on the economy is overwhelming. Its impact derives not only from the scale of the expenditure involved but from the way in which the money is spent. Consider government procurement. It is not just about securing value for money. It can significantly affect the attitudes, efficiency and competitiveness of suppliers in the private sector.

3.6 Understanding and improving the relationship between the government and the rest of the economy is therefore critical to improving national performance.

Government's role

- 3.7** Addressing the state of the economy requires action from everybody in the UK working together. While growth is everyone's business, the vision and leadership for the overall direction of our economy comes in large measure from the Government.
- 3.8** The devolution of economic initiative to local leaders described in the previous chapter will necessitate a change in the function and size of central government. But it is not only what government does that matters – it is *how* it does it.
- 3.9** I believe Whitehall should be a smaller, strategic centre with a focus on analysis, diagnosis, strategy-setting and monitoring. It should do less, better. Departments should aim to be centres of excellence with expert knowledge on economic and policy issues. At the same time they should maintain close relationships with business stakeholders and local players as facilitators, challengers and arbiters. Vitally, they must have the confidence to provide clear central direction when it is required.

How government works

- 3.10** Reforming the way Whitehall works is a significant challenge. My 45 years in politics have shown me that successive governments of all colours have failed to address the reality that Whitehall departments – both ministers and officials – too often pull in different directions. They can be resistant to change, take too long to make decisions, devise policy in ivory towers and create uncertainty through repeatedly changing tack. I have heard these views echoed time and time again from business people and, to be fair, by many ministerial colleagues and their officials.
- 3.11** Much needed reform is already taking place. However, the government machine needs to work in a fundamentally different way to deliver growth.
- 3.12** The Government must have a clear blueprint for the future to support wealth creation. This approach should then be applied without exception across the whole of government. Too many in government believe that growth is something for the Treasury or the Business Department to worry about. Every unit of government needs to understand the extent to which it shares this fundamental responsibility.
- 3.13** As a first step, ministers will need to work better across departments so that decisions taken by each department work in tandem and harness the collective power of government to support wealth creation. It is implicit in the reforms I have in mind that there will be consequences for the structure of central government. However, I applaud the determination of this government not to distract itself by rearranging the Whitehall deckchairs. In line with this approach, my view is that it would be better to make any necessary administrative changes in the light of relevant experience rather than holding up the reforms themselves.

3.14 A vital ingredient in moving to a stronger, strategic centre of government is improving the decision-making culture. A complaint often made of this and previous governments, is that it takes too long for decisions to be made. Delays can have a devastating impact on business activity. The next chapter sets out some specific examples of decisions which are in my view long overdue. The Government and the civil service must create the right incentives to ensure decisions are well thought through *and* timely. We must eradicate the scope to kick difficult questions into the long grass. Through the rest of this chapter I set out a new structure to meet this challenge. It will only succeed if it is coupled with a change of mindset from ministers and officials, particularly a much less risk averse approach.

Overarching growth strategy

3.15 The message I keep hearing is that the UK does not have a strategy for growth and wealth creation.

3.16 Since the election, the Government has rightly focused on getting debt under control. The impact of this should not be underestimated – it has helped cut the deficit by 25% and reduced the cost of borrowing. The Government knows that austerity measures alone are not enough to ensure the UK's long term prosperity and steps have been taken to drive economic growth. The May 2010 Coalition Programme²⁷ and the Plan for Growth²⁸ published in March 2011 set out significant action in key areas such as tax, regulation, planning and infrastructure.

3.17 But the key question is the extent to which policy documents of this sort influence the behaviour of the public and private sectors. Put crudely, who knows of them or has changed their behaviour as a consequence? There is a powerful appetite in the business world for the Government to lay down a vision for how we will achieve long term prosperity in the UK and a plan to ensure its implementation through all departments. To be convincing such a plan needs to concentrate on product not just process.

3.18 This view was echoed by the House of Commons Public Administration Select Committee in 2012²⁹ which stressed that: 'National Strategy must remain on a higher level, maintaining clear 'line of sight' with policy and operational strategy (or implementation) below it. National or 'Grand' Strategy must be broader than a single government department, and thus not subject to departmental silos. By its very nature, the national or 'Grand' strategic level must also be long term'.

3.19 A National Growth Strategy must be created in consultation with the business community setting out a progressive vision for wealth creation over the long term. So far as political realities permit, the debate should also include the main opposition parties.

²⁷ *The Coalition: Our programme for Government*, May 2010

²⁸ HMT/BIS, *The Plan for Growth*, 2011, http://cdn.hm-treasury.gov.uk/2011budget_growth.pdf

²⁹ House of Commons, Public Select Committee, *Strategic thinking in Government: without National Strategy, can viable Government strategy emerge?*, 2012

- 3.20** We must not delude ourselves that achieving a vibrant economy capable of sustained growth is something that can be done in a few years or is a simple list of tasks to be worked through. There are no quick fixes or easy wins.
- 3.21** It will of course remain for democratically elected politicians to decide the specific priorities for any one parliament. I will not therefore propose the terms of the strategy in this report. The system I set out in this and the previous chapter can be used whatever the particular economic priorities of a given government – indeed, it is vital that we end the cyclical changes of government architecture and systems that so frustrates the business community. What the strategy must do is set out how the Government itself will:
- > give concrete commitments against which it can be held to account
 - > fully exploit its muscle across the range of its economic activities
 - > work in collaboration with business and its representative bodies across the economy
 - > continuously improve by cutting out failure, building on success, learning from other countries and exploiting opportunities
 - > be an open culture and a centre of excellence – enhancing and embracing the talents and energy of its people.
- 3.22** Critically, the Growth Strategy needs to be more than a management tool for Whitehall departments. It must send a loud and unequivocal message to the country that the Government takes growth seriously and has a credible strategy. At the same time it cannot be set in stone. We live in an unpredictable world and there will be times when plans need to be adjusted – just as business will respond to new threats or opportunities.

Recommendation 16: The Government should produce an overarching and long term National Growth Strategy setting out its vision for wealth creation, with concrete commitments against which it can be held to account.

Leadership and oversight

- 3.23** To be successful, the Government's strategy must be underpinned by a strong governance structure. There is much activity within government to promote growth and there are many clever people at work. I do not believe, however, that current structures do enough to enable the Government to work together coherently to drive through the change required. I therefore believe we need:
- > a new National Growth Council chaired by the Prime Minister, supported by a dedicated secretariat and with a minister appointed to ensure that the Council's decisions are implemented on the Prime Minister's behalf
 - > departments and public bodies publishing their own plans setting out how they will support the Government's overall Growth Strategy

- > a stronger role for Whitehall's Non-Executive Board Members in challenging and scrutinising departmental plans and contributing to the Growth Council
- > effective management and monitoring of government activities, including a new management information system applied across Whitehall to ensure that resources are allocated to priorities and departments are held to account for their performance by Parliament, the public and the Growth Council.

3.24 The importance and scale of this mission means it must be led by the Prime Minister. He should chair the new Council – just as he chairs the National Security Council. The Council should be the Government's single, strategic body for the growth agenda, replacing any existing ministerial committees created to consider growth. It should also oversee the work of committees responsible for policy areas with a strong impact on growth, including the work of the Economic Affairs (Infrastructure) sub-Committee in taking decisions to proceed with major investment projects.

3.25 The National Security Council provides an interesting model. It is a Cabinet Committee chaired by the Prime Minister that coordinates the Government's response to threats faced by the country and brings together the work of relevant government bodies in relation to national and international security. The Growth Council would be the equivalent of the National Security Council, coordinating the Government's response to the economic challenges facing the country.

3.26 In my model, a key role for the Growth Council will be to approve bids from the Local Enterprise Partnerships (LEPs) for funding from the Government's single funding pot. As bids will encompass a full range of local economic activity, the Council will need advice from experts covering a wide spectrum of knowledge and experience. Bids will be evaluated in line with a bidding framework (see Annex E), and an assessment made about how effective they are likely to be in delivering the objectives set out in individual LEP strategies, and in collectively meeting the Government's overall growth priorities.

3.27 Another vital role for the Council will be to speed up decision making. Any issue not resolved by officials within a department in three months should be referred to the responsible minister for a decision. Any inter-departmental issues that are unresolved within three months should be referred to both Secretaries of State. If they do not reach a decision within six months in total, any Secretary of State should have the right to take the issue to the Council.

Government Non-Executives

The Government's Non-Executive Board Members are experts from outside government who sit on departmental boards to support the secretary of state in his or her role as chair of the board. They come from a range of backgrounds with experience of managing complex organisations, in many cases in the private sector.

Non-Executives provide advice and challenge to departments on management and operational issues and the implementation of departmental business plans. A key part of their role is to ensure their department has the capability to meet current and future needs. They also share best practice so that departments learn from the successes and failures of comparable non-government organisations.

Lord Browne of Madingley is the Government's Lead Non-Executive and worked with secretaries of state to appoint Non-Executives to the board of each government department. There are now around 60 Non-Executives, with a lead Non-Executive in 16 central departments. They are appointed by and accountable to the relevant secretary of state.

The Government's Lead Non-Executive meets regularly with departmental Lead Non-Executives, individually and as a collective, and feeds their views back to the Prime Minister, Head of the Home Civil Service, Cabinet Secretary, and Efficiency and Reform Board and to Parliament through an annual report to the Public Administration Select Committee.

- 3.28** The Council itself should be comprised of secretaries of state from the key economic departments, with other ministers attending meetings of the Council on an ad hoc basis to present their growth commitments. The Council should report to the full Cabinet on a regular basis. Each secretary of state should attend, not only to represent their departmental policy interests, but also to maintain the profile of local issues at the centre of government through their association with LEP areas. Three or four of the Government's Non-Executives should be permanent members of the Council to provide advice and external challenge. Other experts should be invited to participate in individual discussions to ensure the Council's decisions are well founded.
- 3.29** The Prime Minister has enormous demands on his time and he would clearly not be able to oversee the day to day work of the Growth Council. A ministerial post supported by a strong secretariat should therefore be created to take operational responsibility for the strategy and hold departments to account. The secretariat should draw its staff from across Whitehall augmented by private sector secondees. Government should work with departmental Non-Executives and external stakeholders, particularly from business, to identify suitable nominations.

- 3.30** Such a secretariat could sit in the Cabinet Office, the Treasury or a new unit based in Whitehall. This is a matter for the Prime Minister and will be controversial whichever way it goes. However, recent developments indicate a starting point which seems to make sense to me.
- 3.31** Rather counter to my experience of traditional Treasury practice, it is now taking responsibility for implementing specific policies. Treasury roles now include sponsorship of the financial services industries, cities policy and major infrastructure policy. In addition, following the remarkable success of the Olympics construction project, Paul Deighton is to join the Government as Commercial Secretary to the Treasury in January 2013. It would make sense to seize the opportunity to expand this team and charge it with ensuring the timely implementation of the Growth Strategy. This would leave responsibility for individual policies where they lie now, with departments, but it would throw the unified resource of government behind their implementation.

Recommendation 17: A new National Growth Council should be established, chaired by the Prime Minister and with a strong, cross-government focus on driving growth and wealth creation.

Recommendation 18: Operational responsibility for implementation of the National Growth Strategy should rest with a designated minister, supported by a secretariat.

- 3.32** The Prime Minister already has a Business Advisory Group made up of about 20 business leaders. This should continue. One of its key roles going forward, however, should be to provide the Growth Council with regular analysis and advice on critical business and economic issues. This would be similar to practice in the US.

The President's Council on Jobs and Competitiveness

'The walls of the echo chamber can sometimes keep out fresh voices and new ways of thinking – and those who serve in Washington don't always have a ground-level sense of which programs and policies are working.'

President Obama

The Jobs Council was created to provide non-partisan advice to the President on strengthening the US economy and ways to create jobs, opportunity, and prosperity. Modelled on the Foreign Intelligence Advisory Board, it is meant to disrupt the potentially insular federal policy process. Chaired by Jeffrey Immelt, CEO of General Motors, the Council is made up of distinguished business leaders and academics. It is mandated to:

- solicit ideas on how to bolster the economy
- report directly to the President on the design, implementation, and evaluation of policies to promote the growth of the American economy
- provide analysis and information with respect to the operation, regulation, and healthy functioning of the economy.

The Council has made 90 recommendations for action by the federal government in areas such as infrastructure, tax, regulation, education, skills and innovation. The President has implemented 54 of 60 recommended executive actions, while six of the 30 legislative proposals requiring Congressional action have been implemented.

- 3.33** To ensure there is an unrelenting drive to implement the Growth Strategy, a shadow committee of permanent secretaries and Non-Executives, chaired by the designated minister, should be created. This committee would be responsible for regularly monitoring progress, spotting and resolving problems and where necessary escalating issues to the Council.

Recommendation 19: Government should establish a shadow Growth Council of permanent secretaries and Non-Executives chaired by the designated minister to drive implementation of the Growth Strategy across all departments.

Departmental planning

- 3.34** All parts of government have a role to play in supporting economic growth. The role may be more obvious in some government departments than in others, but wealth creation should be, in part, the business of *all* departments.

- 3.35** I was disappointed, but not surprised, to find that most people I spoke to thought departmental business plans were not fit for purpose. These documents collectively list some 1,200 actions and over 600 milestones. They do so without providing any sense of scale, priority, linkages or intended outcomes. I am pleased to see that the need for reform has already been recognised and welcome the action being led by the Minister for Government Policy and the Government's lead Non-Executive.
- 3.36** To make the system effective, there are a number of essential pre-requisites.
- 3.37** Each department must analyse how its policies affect growth and how it can contribute to the growth agenda. This should include how it will use the economic levers at its disposal to stimulate the economy. It should do this in discussion with ministers and Non-Executives. Departments should consider the complete horizon of potential growth areas, in particular those that are not part of their core business. For example, each department's chief scientist could provide valuable insights, including harnessing the Technology Strategy Board and Research Councils' assessment of UK research strengths. Every department's business stakeholders will also have a view.
- 3.38** This analysis should feed into the production of a departmental growth commitment which articulates how departmental policies align with the government's wealth creation agenda, creating a clear line of sight to the Growth Strategy, and sets out specific growth-related outcomes, with anticipated impacts and deadlines. This should include actions delivered by quangos and objectives shared with other government departments.
- 3.39** Departments should include these commitments in their annual business plan and each year report on progress made against them (including how they used their economic levers), the consequences for the growth agenda and commitments for the coming year. Growth commitments and business plans should be published.
- 3.40** The role of Non-Executives should be strengthened and formalised so they are involved throughout the development of departmental growth commitments and business plans. If they consider their views are not being taken into account this should be referred to the shadow committee of the Growth Council. Non-Executives should have access to the Growth Council secretariat to support their enhanced role. Departments must, of course, be careful to avoid any conflicts of interest resulting from this expanded role for Non-Executives.
- 3.41** The secretariat to the Growth Council should provide robust challenge to departments to ensure the efficacy of their plans and their implementation. Crucially the secretariat will need to ensure that the plans collectively create a coherent whole to deliver the Growth Strategy.

Recommendation 20: Departments should include a growth commitment in their annual business plans setting out their contribution to the Growth Strategy over the previous year and planned action for the coming year. This should explicitly include how departments have used the economic levers available to them to support growth over the long term.

Recommendation 21: The role of Non-Executives in the development of growth commitments and departmental business plans should be strengthened and formalised. Non-Executives should have access to the Growth Council secretariat to support their enhanced role.

Business planning in public bodies

- 3.42** A huge amount of government business is undertaken by public bodies. These bodies have many titles – executive agencies, regulators, quangos. It is important that all these bodies support growth, working with their sponsor departments and government as a whole.
- 3.43** Work overseen by the Minister for the Cabinet Office has resulted in a 10% reduction in the number of non-departmental public bodies (NDPBs). Those bodies that remain will be kept under close scrutiny through triennial reviews, including examining whether the NDPB's functions could be better delivered by other means. In line with the principle of devolution, I believe each review must also assess whether any functions could be better carried out at a local level. A new management information system should support these reviews by shining a light on responsibilities suitable for enhancement, reduction, outsourcing or transfer to localities or the private sector.

Recommendation 22: Departments should work with the public bodies they sponsor to ensure they explicitly consider their potential for supporting wealth creation when developing business plans.

Recommendation 23: Government must continue to look at opportunities for devolving or transferring the functions of public bodies to the local level or to the private sector.

Management information

- 3.44** Government's business planning process must be underpinned by effective management information, monitoring and accountability. Departments must have a tighter grip on how they spend their budgets and the connection between cost and output, and output and impact. This is how large corporations are managed. Departments should be run in the same way.
- 3.45** When I was Environment Secretary in the early 1980s, I implemented the Management Information System for Ministers, known as MINIS. This system provided details of the financial and human resource allocated to each departmental programme, as well as the outcomes and impacts. MINIS provided invaluable information to ensure that the department's resources were properly matched to its priorities.
- 3.46** A number of reports in recent years have pointed out the potential for government to generate significant efficiencies and savings through the effective use of management

information. As far back as 1982, the Treasury and Civil Service Committee³⁰ recommended that the MINIS system or an equivalent should be adopted in all Departments and other public sector bodies.

- 3.47** Ministers or permanent secretaries cannot know what their civil servants do, how much it costs, who authorised it, what output measures have been set or, crucially, whether they are being met. My scepticism is based on the simplest of reasons. There are no management information systems in place that enable them to do so.
- 3.48** In his 2012 Annual Report³¹, Lord Browne, the Government's lead Non-Executive, made management information one of his priorities for 2012/13. He stated that 'good management information is a vital means to an end for improving performance and contributing to the transparency agenda'.
- 3.49** A single departmental management information system for Whitehall should be introduced as soon as possible. If done properly, it will be possible not only to cost activities and monitor progress against priorities, but also to provide for much more comprehensive scrutiny and the identification of activity that could be delivered more effectively by the private sector. This is not just a cost cutting exercise. It will reveal areas where important tasks are not being effectively carried out and need more resource.
- 3.50** I am encouraged by the commitment in the Civil Service Reform Plan³² to put in place 'a robust cross-government Management Information (MI) system', as long as the new system integrates financial and personnel data. Annex F sets out the key principles of such a system and how it should look.
- 3.51** Public bodies – or quangos – play a significant role in the public sector. They deliver key services, perform important functions and administer huge sums of public money. These bodies must therefore be subject to the same discipline as central departments in using high quality management information.

Recommendation 24: A Whitehall management information system must be introduced and should encompass management and financial data as set out in Annex F.

Management and accountability

- 3.52** I am not naïve enough to think that simply introducing a fit for purpose management information system will be sufficient. To be truly effective, management information needs to be demanded and used by ministers, permanent secretaries, departmental boards and

³⁰ Efficiency and effectiveness in the civil service, Third Report from the Treasury and Civil Service Committee, Session 1981/82

³¹ *Government Lead Non-Executive Annual Report*, Financial Year 2011/12, <https://update.cabinetoffice.gov.uk/sites/default/files/resources/Government-Lead-Non-Executive-Annual-Report-2011-12.pdf>

³² HM Government, *The Civil Service Reform Plan*, June 2012, <http://www.civilservice.gov.uk/wp-content/uploads/2012/06/Civil-Service-Reform-Plan-acc-final.pdf>

parliamentary committees. The reforms outlined in this report involve changes to roles and responsibilities in central and local government and arm's length bodies. It will be for the government to put in place a system that creates clear lines of accountability and ensures ministers, top civil servants and parliamentarians have a vested interest in having access to high quality management information.

Unleashing public sector enterprise

- 3.53** Our civil servants are often at the wrong end of bowler hat jokes. We rarely hear of the many examples where they have shown drive and ingenuity to transform services. Most people have the capacity to be enterprising and inventive given the right circumstances – this includes public servants. However, the culture and work of the public sector has always had inherent restrictions that discourage risk taking and shackle innovation. We must look at ways to unlock the latent potential in public servants.
- 3.54** I instigated a large number of government privatisations. Indeed, I believe it is the case that I have been responsible for more privatisations than any other minister. I have seen time and again the transformative effect on public servants of the opportunities and ethos of the private sector. The Laboratory of the Government Chemist (LGC) was until 1996 an arm of the Department of Trade and Industry. Today it is owned by its management and staff. Since privatisation, LGC has significantly expanded its activities. It has grown both organically and through acquisitions. Its turnover in 2010/11 was £130.6 million, up from £15 million in 1996/97, and staff numbers rose from 273 to 1,380 in the same period.
- 3.55** Moorfields Eye Hospital has demonstrated how it is possible to sell the expertise of our public services overseas. It has had a branch in Dubai since 1997 which earns much-needed revenue to reinvest in its UK services. The Government is looking at other opportunities for NHS healthcare services in growing markets such as India and China. I commend this initiative.
- 3.56** In Cleveland, firefighters have taken ownership of their brigade and now run it as a mutual business. It is a community interest company and provides fire and rescue services under contract to the local fire authority. It also provides services to the private sector in order to subsidise its work for the public. It won its first contract in July 2012 to provide 24-hour emergency cover to a local plastics manufacturer. The Brigade received £95,000 from the Government's £10 million Mutual Support Programme which helps mutuals get up and running.
- 3.57** The public sector at large should think creatively about how it can pursue similarly enterprising ideas. I commend the Cabinet Office's Mutual Support Programme and its Better Business Models agenda which seeks to reform the delivery of public services by introducing ownership structures to unlock innovation and talent across public services. I would raise just one caveat: beware the unaccountable quango. Whoever provides public services with taxpayers' money must be clearly accountable for their actions.

Getting the right mix of skills

- 3.58** As well as efficient structures and systems, any large organisation must have the best people in place to meet its objectives.
- 3.59** The UK's civil service has a deserved, worldwide reputation for integrity and impartiality. It now faces the challenge of adapting to an ever more competitive and changing world.
- 3.60** Central government is responsible for a wide range of policies and has to interact with a large number of interested parties – in roles such as policy maker, regulator, sponsor and procurer. The civil service must therefore be equipped to understand and interact with the world in which it plays so influential a role.

External appointments

- 3.61** Creating a smaller, more expert central government that embraces a range of disciplines will inevitably require changes to how the civil service recruits and manages its people. Recruitment practices must bring in new entrants of the highest calibre, and effective staff management should encourage strong performance and tackle poor performance, including dismissing consistently poor performers. I, therefore, applaud the Civil Service Reform Plan's ambition to create 'a modern employment offer for staff that encourages and rewards a productive, professional and engaged workforce'.
- 3.62** For many, recruiting experts into government is a controversial proposal. It will mean looking at issues such as public sector pay freezes, redeployment pools and recruitment restrictions. The Cabinet Office is leading a review of terms and conditions in departments so they reflect good practice in the wider public and private sector. This won't be easy, but it is critical for any successful organisation to recruit and retain top quality people. We cannot have a situation where government departments are not able to secure the people with the skills and expertise they need.
- 3.63** The Government is in an invidious position. It has to make urgent and unavoidable cuts, yet in many places it needs greater expertise that can only be obtained by recruiting from the private sector at levels of remuneration that are significantly higher than civil service pay scales permit.
- 3.64** Public procurement is a good example of an area where there is an urgent need for experienced professionals. This issue is discussed in the next chapter – but, in short, I believe difficulties with pay policy should not prevent the government finding a solution to this problem. Part of the solution should be departments getting the skills they need within their total salary budget, rather than focusing on pay scales and staff numbers.

Recommendation 25: The Cabinet Office should work with departments to remove restrictions on departments recruiting externally for key skills and professionals – including disapplying general pay ceilings, recruitment freezes

and redeployment pool policies. In making recruitment decisions, departments should focus on controlling their total salary costs. Where a recruitment breaks a pay ceiling, departmental Non-Executives should give their approval to the process and the appointment.

3.65 For the most senior civil servants the Civil Service Reform Plan sets out proposals for a stronger role for ministers in the recruitment of permanent secretaries and a continued role for Non-Executives as members of selection panels. I would go a step further and give Non-Executives the power to make recommendations on the appointment of permanent secretaries.

Recommendation 26: Departmental Non-Executives should be able to make recommendations on the appointment of permanent secretaries.

Secondments

3.66 An invaluable way of creating cross fertilisation between the public and private sector is through secondments. It is essential that secondees can be brought in to serve in an executive as well as an advisory capacity. They must be able to manage and direct people and budgets. During my time as President of the Board of Trade, I took steps to ensure there was a good flow of people between the department's sector sponsorship teams and the private sector. I understand there are now fewer of these exchanges across central government.

3.67 Evidence received during the review shows that civil service secondees into business obtain invaluable insights into how business operates and find the experience extremely beneficial. The evidence also highlighted a number of problems with secondments:

- they are often viewed by departments as an unaffordable luxury with the added risk that talented staff may not return
- by contrast, many civil servants take the view that going on secondment not only means out of sight, out of mind in career terms, but fear there may not be a job to come back to when the secondment is completed
- where secondments happen, they tend to be at the instigation of the individual rather than the department, and rarely part of a career development plan
- when civil servants return from a secondment, there is often little or no attempt to accrue the full benefit from the knowledge and skills they have gained.

3.68 It is clear that these problems must be overcome if the Civil Service Reform Plan ambition to make 'it easier for staff at all levels to move between the civil service and the private sector' is to be fulfilled. That ambition is essential to creating a credible partnership between government and business to drive growth.

3.69 A debate continues as to whether secondments should be centrally managed or organised by departments themselves. I am neutral on the issue. The important thing is that secondments should happen, are well managed and are long enough to be effective, but not so long that the individual concerned loses touch with their host department. Secondments of a year are probably optimal but in any event should always be more than six months. It is also desirable that staff come back to a role that makes use of the skills and expertise they have acquired.

3.70 There are examples where the secondment model is being rejuvenated. The Cabinet Office recently ran a successful pilot involving civil servants and large public sector suppliers. The programme is being rolled out more widely, recognising the value of seconding staff to organisations that are directly relevant to the department's responsibilities.

Recommendation 27: Barriers to secondments between the public and private sectors should be removed and secondment programmes in government departments should be reinvigorated.

3.71 In addition to secondments there are other ways in which civil servants can gain valuable contact with the business world. For example, the Enterprise Directorate in the Business Department runs a week in a small business programme for its staff designed to provide concentrated time in a commercial environment where it is not practical to go on a long secondment. The Business Department also runs regular staff events with guest speakers from industry. I would commend both of these initiatives to other departments and public bodies.

Civil service training

3.72 Another fundamental way to help people in the public sector to understand the private sector better is through shared learning and development. This is recognised in the Civil Service Reform Plan which outlines how Civil Service Learning – the organisation responsible for procuring learning products for the civil service – will enable staff to undertake learning and development alongside peers from the private and other sectors. The proposal focuses on participants in the Graduate Fast Stream and Senior Civil Service development programmes. I encourage the Government to open up these opportunities to as broad a range of people as possible.

Recommendation 28: Civil Service Learning should develop courses aimed at encouraging public and private sector people at all levels to train together.

3.73 In addition, programmes of specialist training could contribute to a smaller, more strategic centre of government. As the Civil Service Reform Plan rightly points out 'without the right skills and capabilities the civil service will struggle to deliver the Government's priorities effectively'. The reform plan initiated the development of a five year capabilities plan for the whole civil service and a new Civil Service Competency Framework to be rolled out from

April 2013. These initiatives should be seen through to fruition and success and avoid the fate of the previous Professional Skills for Government agenda which fell by the wayside.

- 3.74** We are not the only country in the world grappling with the challenge of retraining public servants for the future. In implementing this programme of training, Civil Service Learning would amass a considerable knowledge base. It should use this know how to transform itself into a centre of excellence and a global leader in training civil servants. There is a unique opportunity to spin out Civil Service Learning into a commercial entity and for it to export its products and services to governments all over the world.

Recommendation 29: Civil Service Learning should be recreated as a commercial body to train civil servants to perform more strategic roles and develop expert policy knowledge, and to market its services overseas.

Building strong partnerships with business

- 3.75** If civil servants are to play their full part in delivering growth, they must have a constructive relationship with business. Too few people in the public sector understand the private sector and in some cases distrust business motivations.
- 3.76** In addition, too many officials appear to think it is not their job to consider how policy decisions will affect business. In contrast, I have been told that civil servants in Germany start from the position that supporting industry is their bread and butter.
- 3.77** Civil servants should look to work in partnership with the private sector rather than keeping it at arm's length. This relationship should be based not simply on reacting to the latest lobbying campaign, but working with businesses on an ongoing basis to create the conditions for success and challenging them to improve their long term competitiveness.

Relationship with sectors

- 3.78** If this is true generally, it is certainly true in the relationship with the main sectors of our economy.
- 3.79** In drafting this report I am all too aware of industrial policies that have so often in the past failed. That is not what I have in mind.
- 3.80** The concept of industrial strategy for the UK has traditionally been controversial. However, demands for such a strategy have become stronger. They are being articulated from across the political and business spectrum as the scale of the global competitive challenges facing us has become increasingly apparent. When the CBI, the TUC and The Times newspaper are united in calling for an industrial strategy, the issue deserves serious consideration. It seems to me that the sceptics ignore the common practice of our competitor economies.

Dutch 'Top Sector' policy

In February 2011, the Dutch Government introduced a new policy to promote innovation and strategically important economic sectors. Led by the Ministry of Economic Affairs, Agriculture and Innovation, it involves the selection of nine industrial sectors – in which the Netherlands holds a strong international position – to be stimulated by greater investment and R&D tax-reductions. The top sectors are:

- > agri-food
- > horticulture and propagating stock
- > high-tech materials and systems
- > energy
- > logistics
- > creative industry
- > life sciences
- > chemicals
- > water.

Each sector has an innovation hotspot in the Netherlands in which companies and research organisations work closely together. For example, the centre of commercial and scientific activities for high tech systems and materials is Brainport, Eindhoven.

The top sector approach aims to create a strong exchange by bringing together representatives from businesses, knowledge institutes and the Government (the 'golden triangle').

They have jointly identified the problems and opportunities for each sector resulting in the development of action plans covering policy areas such as education, research, overseas trade and environment, as well as action to make the sectors more sustainable. They also focus on attracting European HQs and promoting the Netherlands as the Gateway to Europe, with a focus on the digital economy.

'Innovation contracts' have also been agreed setting out the financial arrangements between businesses, scientists and the Government. Altogether €2.8 billion will be invested in the top sectors in 2012. Industry will contribute €1.8 billion. The Government will invest €1 billion through funding from the Netherlands Organisation for Scientific Research and other research and technology organisations and institutes.

- 3.81** Whenever the words industrial strategy are uttered the retort of interventionism and picking winners is usually not far behind. But what is the alternative; to start picking losers? And what of other governments? In the next chapter I outline how other countries make major procurement decisions with one eye firmly on industrial capability and their national interest.
- 3.82** The Government has myriad choices about where it spends its money so it will inevitably make decisions. In fact, it is already picking winners each and every day through the billions of pounds it spends on, for example, regional programmes, export assistance, access to finance, defence spending and the many business support schemes that it runs.
- 3.83** Equally controversial is the concept of government departments sponsoring sectors. Throughout the review, businesses have told me time and again that they want to have a single route into government and for civil servants to understand their issues and address them in a joined-up way. Many parts of government will say they do this already. I contest that – they do not.
- 3.84** I strongly support businesses' calls for a meaningful dialogue with government. I believe government's relationship with business should be neither a lobbying exercise nor an imposition of government policies on business. What is needed is a mature dialogue with mutual understanding and shared ownership of outcomes. This ongoing dialogue should cover matters such as the drive to expand exports or attracting inward investment, workforce skills, the value of supply chains or industrial clusters, the relevance of standards, effective delivery of government services and the lessons to be learnt from overseas.
- 3.85** I welcome the announcement made by the Business Secretary in September outlining his vision for the future of British industry. The commitment he made to establishing government and industry partnerships for specific sectors and co-creating sector strategies is a very significant step in the right direction.
- 3.86** The analytical paper published alongside the industrial strategy sets out a spectrum of support for different sectors.

Table 3.4: Spectrum of support for different sectors

Light touch	Action	Sustained dialogue	Strategic Partnership
Government sets the environment through horizontal policies (e.g. tax, IPR, skills)			
	Government takes action to respond to specific issues (e.g. tourism in 2012)		
		Sustained dialogue and action (e.g. sector councils, joint strategies)	
			Strategic long term partnership

Source: BIS Economics Paper No.18 – Industrial Strategy: UK Sector Analysis³³

3.87 I see the merits of a banded approach, but it must be quickly enacted and not just for the sectors for which the Business Department is responsible. The Department of Health should have a relationship with the care sector, DEFRA with the water industry. Far too few departments actively work with the sectors of the economy for which they are responsible. This should change. The Government should be bold and introduce:

- > a whole of government approach to sector relationships, reconciling conflicting departmental objectives to create a coherent government position
- > an Industry Council for all major sectors of the economy
- > stronger relationships with lead trade associations
- > an expanded strategic relationship management of key companies
- > knowledgeable civil servants in sector teams able to deal with the private sector as critical friends.

3.88 Every government department should offer a relationship to each sector of the economy for which it is responsible and agree with them an appropriate level of interaction. Departmental Non-Executives should be included in these discussions to offer an independent perspective. The final decision must be endorsed by the Growth Council to ensure there is full sectoral coverage and that a consistent approach is being taken across government. The key elements of each of these relationships should be presented in the departmental growth commitment.

3.89 Where a sector decides not to establish a formal partnership with government, it should not be seen as a licence to ignore them. There still needs to be a Whitehall official who is responsible for connecting the sector with government and this should be set out in departmental plans.

³³ BIS Economics Paper No.18 – *Industrial Strategy: UK Sector Analysis* <http://www.bis.gov.uk/assets/Biscore/economics-and-statistics/docs/1/12-1140-industrial-strategy-uk-sector-analysis.pdf>

- 3.90** I endorse the idea of co-created sector strategies. Where these are established they should set out how government and sectors will work together across the full range of economic activity. Departments should ensure they use and align all the levers at the government's disposal to support their sectors.
- 3.91** Although I believe most funding for business support should be devolved to LEPs to spend in accordance with their individual economic strategies, there will be some need for central government to provide support for particular initiatives derived from the jointly-owned strategies with strategically important sectors. By being much more disciplined and selective about what it does, central government will be able to free up resources to support this work where needed.
- 3.92** Sector teams have a crucial role to play. They will have to act as an advocate and facilitator for their sector, whilst at the same time having the know how and credibility to challenge and work with a sector to enhance its long term competitiveness. Consequently, the teams will need to have people with business expertise, in particular through incoming and outgoing secondments with the private sector. This approach is common practice in competitor economies.
- 3.93** The concept of 'sponsoring' a sector is not well-established in all parts of government. So developing this new approach will require the recruitment of people with the necessary experience in those parts that have not traditionally undertaken a sector sponsorship role.

Recommendation 30: Government departments should offer all major sectors of the economy the opportunity to form a relationship with government.

Recommendation 31: The Department and the sector should agree an appropriate level of interaction which is endorsed by the Growth Council. Each relationship should be set out in departmental growth commitments.

Recommendation 32: Lead departments should coordinate the Government's interaction with each sector, ensuring there is a constructive dialogue with mutual understanding and shared ownership of outcomes.

Industry Councils

- 3.94** The proposals set out here are not new. They exist already as best practice in some sectors. The only innovation is the idea that existing best practice should be the norm.
- 3.95** Where a partnership is established, the lead department should ensure all parts of government align and coordinate their different dealings with the sector so there is a single coherent government voice in each case.
- 3.96** The Automotive Council, with its clear plan and priorities for engagement, is often cited as an example of a successful strategic partnership model between government and an industry sector. Other positive models exist in the aerospace and the life sciences sectors.

Automotive Council

The Industry-Government Automotive Council was set up in 2009 to develop a strategic, continuous and collaborative conversation between government and the automotive industry in the UK. The Council is co-chaired by Business Secretary (as BIS is the sponsor department for the sector) and a leading industry representative. Membership of the Automotive Council reflects the strength and breadth of the UK automotive industry at the highest level.

Through the main ministerial council and two sub-groups on technology and supply chains, it has the active participation of the CEOs and key decision makers of the UK's major automotive manufacturers, suppliers, engineering consultancies, technology developers and academics and helps to join up the historically fragmented and increasingly foreign-owned UK auto industry. The lead trade association, SMMT, runs the Council's website and also produces a monthly newsletter and its CEO sits on the Council.

The Council's remit has been to identify and implement a strategy for the UK auto sector, based principally on the following three elements:

- > **A technology roadmap** and analysis, through which the whole UK sector has committed to supporting the development and use of a common set of generic low carbon and intelligent mobility technologies. The ambition is to exploit UK leadership and capability to promote the UK as a strong investment case around a number of strategic technologies.
- > **Supply chain development** through the evaluation of the total demand picture together with expected forward growth. A detailed survey and analysis has been undertaken in conjunction with the University of Cambridge, and recently updated to reflect £6 billion of new investment by vehicle makers in the UK. This has identified £3 billion of incremental opportunities for local supply spread across a wide range of component categories. Work is in hand to leverage the significant new business opportunities for the UK, for both existing auto suppliers and those seeking to invest in the UK.
- > **Developing overseas networks** and promoting the UK as a dynamic and attractive location of choice for internationally mobile automotive investments, building on critical UK automotive strengths and successes.

3.97 An industry council model should be put in place for every sector partnership. The Automotive Council model is suitable for sectors requiring an intensive, ongoing dialogue with government, but it will not necessarily be suitable for all. Sectors are not homogenous, and departments and sectors will need to determine which model works best for them.

Recommendation 33: An Industry Council should be established for each formal partnership between government and a sector.

Trade associations

- 3.98** Specialist trade associations are important in bringing together groups of companies with common interests and concerns. They provide a coordinated voice for sectors when talking to government so that sector needs and demands can be articulated. Thus they can help ensure that government decisions in areas such as regulation and skills take heed of the impact on particular sectors. As with local economies, a simple act of government can have a differential impact on different sectors of the economy. Government needs this understanding if it is to act effectively.
- 3.99** Trade associations clearly have a key role to play in improving government’s engagement with business sectors. The problem is the reality on the ground. In general sectoral representation in the UK is fragmented, duplicative and often poorly resourced. There is no legislation governing trade associations and no requirement on them to be registered. Anyone can set one up.
- 3.100** The result is a proliferation of bodies of variable quality. The Trade Association Forum estimates that there are currently as many as 3,500 trade associations in the UK. There have been various attempts to address the problems of business representation dating back to the Devlin Commission in 1972³⁴, but the issues of fragmentation and proliferation are still very much alive today. There has been little effective action to address these issues since that report.
- 3.101** Many of these issues are for business to sort out for itself – I discuss this further in Chapter 5. However, through the way it chooses to engage with sectors, government can provide powerful incentives for trade associations to improve and rationalise.
- 3.102** First it needs to reintroduce the concept of lead associations. This would require government to nominate a trade association as the focus for its engagement with a particular sector. Government would then channel all of its engagement, such as consultations, through the lead association. Permanent secretaries and ministers should specifically ask whether policy has been developed in consultation with the lead association. This does not involve any sort of veto on government policy. It is designed to ensure a deeper understanding of the issues and opportunities involved. It simply ensures, as a minimum, proper consultation. Again it is common practice overseas.
- 3.103** A condition of nomination must be that the lead association takes on responsibility for ensuring that the views of the entire sector are fairly represented, and that steps are taken to draw all trade associations operating in a particular sector into new, more strategic working arrangements. This can be done, not only through mergers, but through the

³⁴ The Commission had the terms of reference to review the state of industrial and commercial representation in the United Kingdom.

creation of umbrella bodies. The creation of the Construction Products Association is an example of what is possible³⁵. So too is the formation of ADS in 2009 through the merger of the Association of Police and Public Security Suppliers, the Defence Manufacturers Association and the Society of British Aerospace Companies. It would be a welcome initiative if industry more widely examined the plethora of such bodies with a view to streamlining and improving focus where appropriate. In the end they are paying for these bodies and should ensure that they are getting the best value for money.

- 3.104** Where there continue to be a large number of trade associations, government needs to be ready to enter into a dialogue with the sector to see if so many are needed.
- 3.105** Second, each department with lead responsibility for engaging with a sector needs to have a relationship manager able to act as a critical friend to the trade association, and able to assist it in driving up standards of representation. They should be prepared to give informal feedback on the trade association's performance, such as on the quality of its Budget representations, or being honest when duplication within the industry is proving unhelpful.
- 3.106** I introduced the concept of lead associations in the 1990s but it did not survive. This stop, start approach does not work. Effective trade associations can make a major contribution to the development of productive partnerships between government and the private sector. They are a prize worth striving for, but they need nurturing. The point has been made to me that government gets the trade associations it deserves. If it wants to see trade associations raising their performance, government needs to show a consistent approach and a sustained commitment to joined-up partnership working.

Recommendation 34: Government departments and industry sectors should jointly nominate lead trade associations to represent sectors in their dialogue with government and encourage the private sector to bring about a major rationalisation of trade associations to enhance the quality of the debate.

Strategic Relationship Management

- 3.107** In addition to engaging with specific sectors, successive governments have always developed a direct relationship with individual companies of strategic importance to the economy.
- 3.108** UK Trade and Investment currently oversees a Strategic Relationship Management (SRM) system involving some 50 companies. Through this a company is allocated a lead minister and a top level civil servant to help resolve significant issues. The minister is supported by a virtual cross-departmental team which agrees an account plan with the company and ensures efficient information sharing.

³⁵ The Construction Products Association represents 85% by value, of all manufacturers and suppliers of construction products in the UK, including 24 of the largest companies in the industry, as well as 42 trade associations.

3.109 Feedback from a number of companies who have such a strategic relationship with government indicates that government's performance in these relationships is very mixed, with varying levels of buy-in from departments. There are also limitations to the system in that its original driver was principally to encourage inward investment and it therefore does not currently cover many UK-headquartered companies.

3.110 The Government should build on the SRM system, by embedding it fully in all departments and increasing the number of companies included. Each government department should identify its key companies and take responsibility for managing the government relationship, based on the UKTI model. Departments should select companies based on criteria such as:

- > companies with significant investments in the UK and the possibility of further investment
- > UK-based companies with large overseas operations and the potential for significant export growth
- > companies where government can add most value, including where operations are significantly impacted by the activity of multiple parts of government
- > companies that are strategically important to key UK sectors
- > companies with a product that has considerable potential in high growth markets.

Recommendation 35: Government should increase the number of companies managed through the Strategic Relationship Management model and this should be used by all government departments.

NO STONE UNTURNED in pursuit of
GROWTH

Chapter 4:

Government and growth – catalyst, enabler, partner

- 4.1** For any economy to remain globally competitive there are certain enabling conditions which governments must ensure function properly and help to promote business and growth. The Business Secretary's speech of 11 September³⁶ on the Government's Industrial Strategy indicates the scale of the step change required throughout government. He spoke of 'support for sectors; clear choices and backing for core emerging technologies; continued efforts to boost skills; and extracting the maximum value from the Government's position as a market-shaping customer'. He could have named many more challenges. This ambition cannot be achieved from the Business Department alone. It needs each and every secretary of state to take up the challenge to work more closely with business to deliver growth.
- 4.2** There are two perspectives from which to view the achievement of growth. The first is best driven by local leaders – public and private – working in partnership together to effect the long term changes their communities need. The second starts with the vital responsibility of central government in creating the conditions for economic success. Too often Whitehall departments fail to achieve the full economic benefit of their policies and spending. Or conversely, fail to realise that their actions across the full spectrum of government have an enormous impact – positive and negative – on the economy.
- 4.3** Plainly, one of government's most powerful economic levers is its tax policy. I strongly support the Government's economic strategy and in particular its ambition to have the most competitive tax system in the G20. The Chancellor will determine the Government's fiscal strategy. I have made no attempt to do this job for him. I would only say that the principal void in today's investment climate is confidence – and tax changes will have only a limited effect on that.

Government as a market player

- 4.4** The Government's commercial record buying goods and services needs urgent attention. There are two facts which taken together are an example of why Britain is not competitive.
- The public sector now places around £238 billion of contracts with the private sector each year, a third of its total expenditure. In several sectors it is responsible for over 10% of total demand (see Table 4.1).
 - As recently as 2010, prior to the creation of the Major Projects Authority (MPA), two in three major public sector contracts were completed over budget or over time, or both³⁷.
- 4.5** The waste of public money implied by the second point is unacceptable. But for me the two facts tell a much more profound story. What does it say about a swathe of British businesses that going over cost or beyond schedule is the norm? How can British businesses compete globally if they work to assumptions such as these?

³⁶ <http://www.bis.gov.uk/news/speeches/vince-cable-industrial-strategy-september-2012>

³⁷ *NAO Guide: Initiating Successful Projects*, 2011

http://www.nao.org.uk/publications/1012/initiating_successful_projects.aspx

Table 4.1: Government demand as a percentage of total UK demand (selected sectors)³⁸

Sector	% Share of total demand
Education	61.2
Pharmaceuticals	33.9
Scientific research and development services	27.3
Printing and recording services	24.0
Computer, electronic and optical products	19.9
Legal services	18.0
Air and spacecraft and related machinery	14.8
Postal and courier services	13.1
Architectural and engineering services; technical testing and analysis services	8.6
Telecommunications services	7.6
Real estate services, excluding on a fee or contract basis and imputed rent	6.7
Accounting, bookkeeping and auditing services; tax consulting services	6.3
Advertising and market research services	6.2
Computer programming, consultancy and related services	5.9
Whole economy	16.3

Source: BIS calculations based on ONS supply and use data

- 4.6** Recently I saw a prime example of government procurement not working. It is a simple one, indeed one that will make many people laugh, such is the absurdity. But it says a lot about the way departments approach the buying of goods and services through complicated framework contracts.
- 4.7** The Taxpayers' Alliance recently assessed the amount different departments were paying for A4 paper³⁹. Compared to the cheapest – the Department of Health, which paid £8.93 per box of paper – most other departments were spending over £2 more per box. In a

38 For the purposes of government demand we have used the intermediate consumption of the public administration, health, social and residential care and education sectors and the final consumption of local and central government. This table shows total government demand for products of a sector whether provided domestically or through imports.

39 *Departmental Procurement costs Q4 2011*, The Taxpayers' Alliance, <http://www.taxpayersalliance.com/qdsprocurement.pdf>

wonderful irony, it was the Business Department which they said was shelling out the most – £12.43 a box. Based on that analysis a civil servant printing out this report at the Business Department would be doing so at a cost of 22 pence more than a colleague at Health. Efforts to centralise the purchasing of office essentials through the Government Procurement Service do not seem to be working. Departments do not have to opt in to the scheme and even if they do opt in, they can still purchase items on an individual basis at their own discretion.

- 4.8** The Minister for the Cabinet Office has initiated and published a review of public sector procurement⁴⁰, and I support him as he takes this work forward. I applaud, in particular, the creation of the MPA and its role overseeing the 189 largest and highest-risk government projects. However, it can only ever act as a sticking plaster until the fundamental problem is addressed. There are roughly 3,000 large projects being delivered across government, and tens of thousands of smaller projects with a total value of hundreds of billions of pounds each year. The MPA's resources will simply not stretch to oversee more than a tiny fraction of them. Ensuring effective procurement remains an enormous challenge for the Government.
- 4.9** The fundamental problem is one of skills. Despite the drive to professionalise civil servants under the previous government⁴¹, most of those involved in procurement and project management still lack the necessary expertise to manage large projects efficiently and effectively. This problem has been haunting government for decades, and was thoroughly analysed back in 2000 in a now almost forgotten report⁴².
- 4.10** This report set in motion several important developments which are still in use today, such as the role of the Senior Responsible Owner and the process of peer review at key points in a project's lifecycle. But it failed to deliver sufficient improvements in the skills of the civil servants involved, just as the Professional Skills for Government initiative failed to improve procurement or project management skills a few years later. The vast majority of civil servants are still policy thinkers first and project managers a distant second.
- 4.11** This year the Government announced the creation of the Commissioning Academy and the Major Projects Leadership Academy. These will, over time, help inject significant procurement expertise into the civil service ranks. But procurement and project management need to be established as professional cadres within the civil service to ensure the continued professionalisation of these functions and to ensure the right people are in place to deliver.
- 4.12** There is, however, no substitute for specialist, private sector experience of tendering and managing large, complex contracts. The Government's need for expertise is urgent, and cannot wait for training to percolate and skills to improve. There is no alternative in the short term but to bring in the necessary skills from the private sector. The procurement

40 <http://www.cabinetoffice.gov.uk/news/crown-and-suppliers-new-way-working>

41 <http://www.civilservice.gov.uk/about/improving/psg>

42 *Successful IT: Modernising Government in Action*, 2000, http://www.epractice.eu/files/media/media_680.pdf

arms of the best companies are slick, dynamic and forceful operations. They are staffed by negotiators who ensure every contract with their suppliers gives the very best value for money and has the tightest possible delivery requirements. They would eat most people for breakfast.

4.13 Bringing in private sector experts to work with the existing teams in every department will be expensive. Those responsible for large procurements in the private sector are typically paid more than three times the salary of senior civil servants. I am not recommending massive salary increases for civil servants. But in the short term there is an overwhelming need to bring in private sector expertise at competitive rates to fill the most senior levels of public sector procurement. Given the scale of government procurement each year, the benefits this will bring will far outweigh the costs.

4.14 We already have evidence that such an approach pays dividends. A small number of individuals with extensive relevant private sector experience were appointed to the Government Olympic Executive within DCMS to act as the government client and sponsor of the Olympic Delivery Authority (ODA) and its £7 billion construction programme. They were brought in on competitive remuneration packages, outside normal civil service pay scales. Their contribution to the ODA's successful delivery of the Olympic construction programme – on time and under budget – is a testament to the value of appointing a handful of appropriately skilled individuals to act on government's behalf.

Recommendation 36: Every government department should recruit a Chief Procurement Officer at competitive market rates, reporting direct to the permanent secretary, to lead the procurement and delivery of major projects and improve the capabilities of their procurement cadre. The department's Non-Executives should approve the selection process and appointments.

4.15 Equally in the wider public sector, particularly the NHS and local government, work is needed to improve procurement practices. The drive for change has principally been prompted by the need for efficiencies in public expenditure. But the overall focus for procurement must always be to get best value for money for the taxpayer – not always the same as the lowest price. It is important to ensure a consistent approach to procurement across the public sector to make the process as accessible as possible for the business community, particularly our smaller businesses.

4.16 Whilst I welcome the Cabinet Office's procurement reforms I am concerned that they only extend to central government bodies. The NHS and the social care sector offer obvious potential for growth in the UK. Our medical research and pharmaceutical sectors are amongst the best in the world. Our aging population provides an opportunity for government to work with the private sector in developing the most advanced equipment and services to help this important group in our society. Supporting older people to stay in their own homes is inseparable from the use of modern technology. The pressures

on public finances and the Nicholson Challenge⁴³ to the NHS all provide a clear reason why procurement reform in health could both save the NHS money and create new growth areas for the economy. It would also serve the needs of customers – in this case, the patients.

- 4.17** All public bodies must be transparent about their procurement activities and simplify their processes if we are to be confident that value for money is being delivered. Where funding is devolved to LEPs they too should demonstrate that they meet these standards in their own procurement of services. And it is important that best practice is shared and used among all public bodies. For example, I applaud the work Lord Young is doing to champion small businesses⁴⁴ and highlight the improvements needed in procurement – particularly better and more consistent use of pre-qualification questionnaires.
- 4.18** These improvements are needed right across the public sector. But the Government is not able at present to mandate procurement reform to NHS trusts or local councils. The collaborative development of simple strategic guidance for all public procurement is essential. If this approach fails, the Government should legislate.

Recommendation 37: The Cabinet Office should place a general duty on all public bodies, setting out the procurement standards to which they should adhere, by providing a pan-government procurement strategy, legislating if necessary.

- 4.19** Once procurement decisions have been taken, it is important that contracts are well managed – there is just as much value to be lost in poor contract management as in making the wrong decision in the first place. In addition to the urgent recruitment of high calibre procurement professionals into the civil service, there is another way of improving delivery. Outsourcing the contract management of government projects could ensure that those managing supplier performance are focused solely on the contracts and are not distracted by political considerations. There are many reasons why public bodies throw good money after bad in poorly run projects, but none of them should override the basic requirement to drive up performance. Putting contract management – but not the allocation of contracts – into private hands could diminish these excuses and enable government to improve its record in contract management.

Procurement and the industrial base

- 4.20** There is a tension in public procurement where it applies to sophisticated technologies and not commodities such as A4 paper. What is it for?

⁴³ The Nicholson Challenge refers to a set of mandates that have been put to the entirety of the NHS in a drive to find efficiency savings.

⁴⁴ *Making Business Your Business, Supporting the start up and development of small business*, 2012, www.bis.gov.uk/make-business-your-business-report

- 4.21** The simple answer is to secure value for money for the public purse. Who can argue with that? The problem is that it is often equated with short term, lowest cost procurement which ignores the issues about the country's industrial base – the exploitation of R&D, the skills we need and the creation of jobs. It also ignores international practice. No country of which I have any knowledge takes so simple a view. Although crucial in major policy areas such as defence or aerospace, the same issues are everyday challenges for ministers whether they are placing contracts for high speed trains or new IT systems. We are concerned about the destiny of our manufacturing sector but we do not spend enough time exploring the ways government can work to support it.
- 4.22** For specialist technologies, there will often be an overseas alternative available off the shelf – already paid for by overseas taxpayers, in use and demonstrably capable of working. The simple answer of the marketplace will always be to buy the overseas product at the expense of our industrial base. A broader view – recognising the national interest, in particular our sovereign capability – must always be considered. As the Business Secretary said in his recent speech⁴⁵, we need to strike a balance between buying strategically with an eye on long term capability and saving money in the short run by going for the cheapest off the shelf options.
- 4.23** It is not a black and white situation. On the one hand governments have sometimes tried to take into account the impact on the industrial base with less than conspicuous success, thus breeding the argument that we should not indulge in this type of intervention. On the other, governments often bow to political pressure when a noteworthy contract is on the verge of being awarded overseas. These issues are interwoven and should not be dealt with on a crisis management basis in the glare of an indignant press campaign. Every other advanced economy faces these issues and pursues what it believes to be its national self interest. We need to set the slogans aside and establish in the most effective and professional way where our interests lie and then go for them.
- 4.24** Let me illustrate this point. The US directs some \$190 billion a year for procurement, including R&D, through the Pentagon⁴⁶ and some \$16 billion through NASA⁴⁷ which largely ends up in the US industrial base. When President Reagan launched the Star Wars programme, General Abrahamson, Director of the Strategic Defense Initiative, came to see me at the Ministry of Defence. He explained the advantages for the UK if we joined the programme. 'I would be willing to commit today \$100,000', he said, 'to back the research at Heriot-Watt University.' He knew exactly where the leading-edge technological development was taking place and he was systematically offering to establish partnerships in every field. With one major defence initiative, the US was acquiring partnerships with the best brains and leading technological advances in the world to ensure it had the best capabilities at its disposal.

45 <http://www.bis.gov.uk/news/speeches/vince-cable-industrial-strategy-september-2012>

46 *Budget of the United States Government*, Fiscal Year 2011

<http://www.whitehouse.gov/sites/default/files/omb/budget/fy2011/assets/defense.pdf>

47 <http://www.nasa.gov/open/plan/procurement.html>

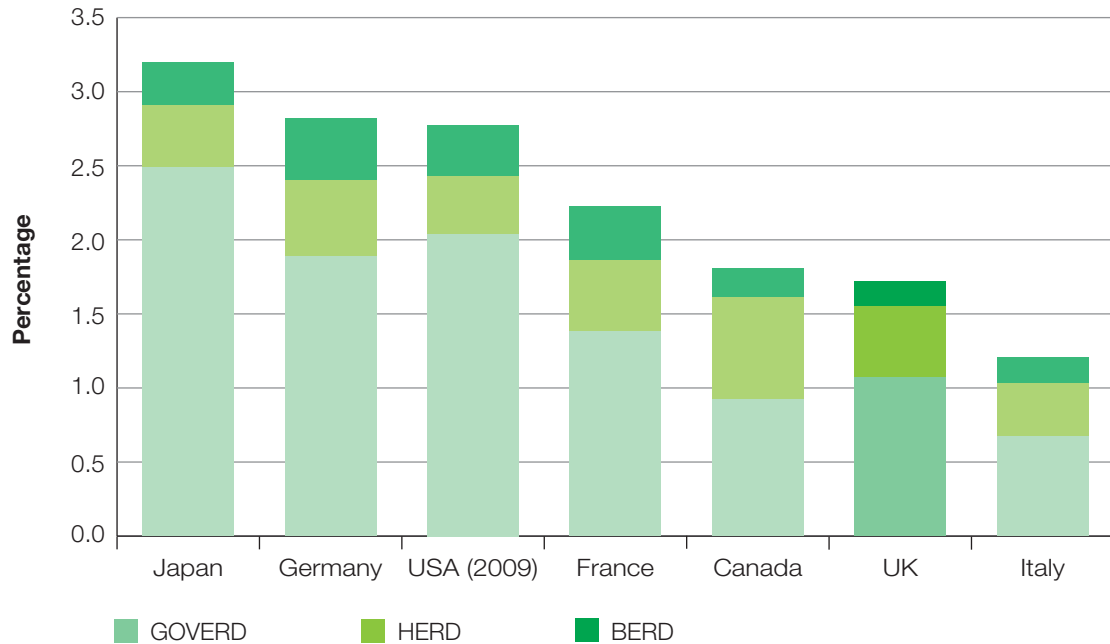
- 4.25** The French use the same technique. They have saved European civil aviation and are the only European country capable of building nuclear power stations or conducting space launches. The Chinese are building the same capabilities and against a strategy I first heard articulated in 1973. If our own government departments do not take a wider national view when procuring such specialist technologies, our capabilities will continue to drift away, damaging UK strategic and economic interests.

Recommendation 38: The Government should go further in its plans to build strategic relationships with industry, ensuring that the long term impact on technological advantage and the UK industrial base are taken into account in the procurement of specialist technologies.

Addressing the challenges of tomorrow

- 4.26** Global competitiveness is not just about working hard and believing we will get there one day. We have to keep looking at our international rivals and learning from them if they do things better.
- 4.27** Innovation and research are vital to the pursuit of excellence. In technology based sectors, research is a primary driver of innovation and the discovery and commercial exploitation of new technologies. In other sectors the rapid adoption of technologies is essential to innovation, sometimes transforming existing industries. In short, the success of our economy depends on the extent to which businesses in all industries and sectors invest in adapting technologies and building innovative capacity in order to get ahead.
- 4.28** The costs of cutting edge research and the latest high tech processes are greater than ever before, and are often too large for any one company to bear. No competitive economy just leaves universities, research laboratories and the private sector's innovation arms to their own devices. Our competitors understand that a country's research and innovation capability is a key part of the national infrastructure. In contrast, the UK spends relatively less on pure R&D compared to its peers. Gross Expenditure on R&D (GERD) as a proportion of GDP was 1.8% in 2010, placing the UK sixth amongst the G7.

Chart 4.1: Sector contributions of Gross Domestic Expenditure on R&D to GDP (per cent, 2010)⁴⁸



Source: OECD Main Science & Technology Indicators

4.29 The UK’s knowledge base – with four of the top six universities in the world⁴⁹ – is a priceless national asset, and a source of international competitive advantage. Higher Education expenditure (HERD) on R&D also shows signs of strength, with the UK ranking third in the G7. The challenge here then is to secure this strength for the long term. We are lucky to have enjoyed cross party consensus on the importance of both strong and stable levels of science and research funding.

Recommendation 39: The Government should continue to commit to the long term stability of the core funding of science and research, at a level which keeps pace with our international competitors.

4.30 The most competitive companies in the world do not just concentrate on selling in their current market – they are busy behind the scenes developing the next generation of products and services. The iPad, iPhone and iPod have blown many of Apple’s competitors out of the water. Its most successful rivals – domestic and international – have stayed afloat by innovating further. But the US Government plays a major role, perhaps greater than recognised, in shaping innovation. In particular it has a systematic

48 Business expenditure on R&D (BERD) covers R&D activities carried out in the business sector by performing firms and institutions, regardless of the origin of funding. It includes both publically and privately funded R&D; Higher Education expenditure on R&D (HERD) includes R&D activities carried out by universities, colleges of technology and other institutions of post-secondary education. It includes both publically and privately funded R&D; Government expenditure on R&D (GOVERD) includes expenditure on R&D performed in the government sector.

49 QS World University Rankings, 2012

and comprehensive approach to driving innovation and supporting small businesses through its Small Business Innovation Research programme.

US Small Business Innovation Research programme

This pre-commercial procurement model has been used successfully in the US since the 1980s. The scheme is designed to encourage small business to develop new processes and products and to produce quality research in support of the US Government's policy priorities. It was introduced due to concerns in the US about:

- the country's ability to compete in the face of Japanese performance in automotive, steel and semiconductors
- failure to translate research prowess into commercial advantage
- the declining share of federal R&D going to SMEs and the problems faced by innovative small business in raising capital. Technology based small businesses employ nearly 40% of the science and engineering workforce in the US and SMEs account for 60-80% of net new jobs created annually.

The programme lets \$2 billion of contracts annually. Since inception the SBIR⁵⁰ programme has worked with over 15,000 firms, developed more than \$21 billion worth of research and over 45,000 patents. Qualcomm and Symantec are often quoted as SBIR success stories. Qualcomm employs some 16,000 people with sales revenue in excess of \$10 billion and a market capitalisation in excess of \$60 billion. Symantec employs 17,000 people with sales revenues in excess of \$6 billion and a market capitalisation in excess of \$13 billion. The Innovation Development Institute estimates that SBIR delivers a multiplier of five to seven in terms of economic benefit accrued.

4.31 As a nation we need to do the same, to ensure UK business can build and take advantage of the technologies of tomorrow – be they high performance computing, synthetic biology or autonomous robotics. As such, I commend the transformative approach of the current Minister for Universities and Science in bringing together government, industry and academia to create joint technology roadmaps – assessing where the relevant technologies are heading over the next five years or so, what publicly funded research is needed to support it, and what business is likely to do. The UK's own Small Business Research Initiative (SBRI) is starting to show potential as an approach for solving public sector challenges while also supporting innovative high growth companies. If we do not invest – public and private sectors – for the long term our economy will pay the price. Catapult Centres are also providing a new national network to act as a bridge between academia and industry to support the commercialisation of new technologies.

50 www.sbir.gov

4.32 We need to ensure that government is doing the best it can to leverage the world renown of the UK research base and higher education sector when marketing the UK overseas. Our world class research base acts as a strong magnet for inward investment – witness the IT cluster which has developed around Cambridge, attracting major investments from Microsoft and Hewlett-Packard among others.

Recommendation 40: UKTI should work with the Technology Strategy Board and the Research Councils to strengthen the marketing of the UK as an inward investment destination on the back of our world-renowned research excellence.

4.33 We need to maximise the benefits of these research strengths to support business led innovation. Global leaders in innovation, such as the US, Japan, Germany and Sweden, have well connected systems that enable the public and private sectors to work together to maximise the economic benefits of innovation. Evidence suggests the UK system is not as well connected or orientated to the needs of business⁵¹.

4.34 UK businesses continue to underinvest in research and development compared to our international competitors. In the UK, Business Enterprise R&D (BERD) as a proportion of GDP has remained below that of other leading economies such as Japan, the US, Germany and France over the last two decades⁵². Further, there has been a slight downward trend in BERD intensity in the UK since 1990, while most advanced economies – except Japan – have experienced fairly steady levels. We therefore need to better combine public and private investments in innovation to ensure we do not fall behind.

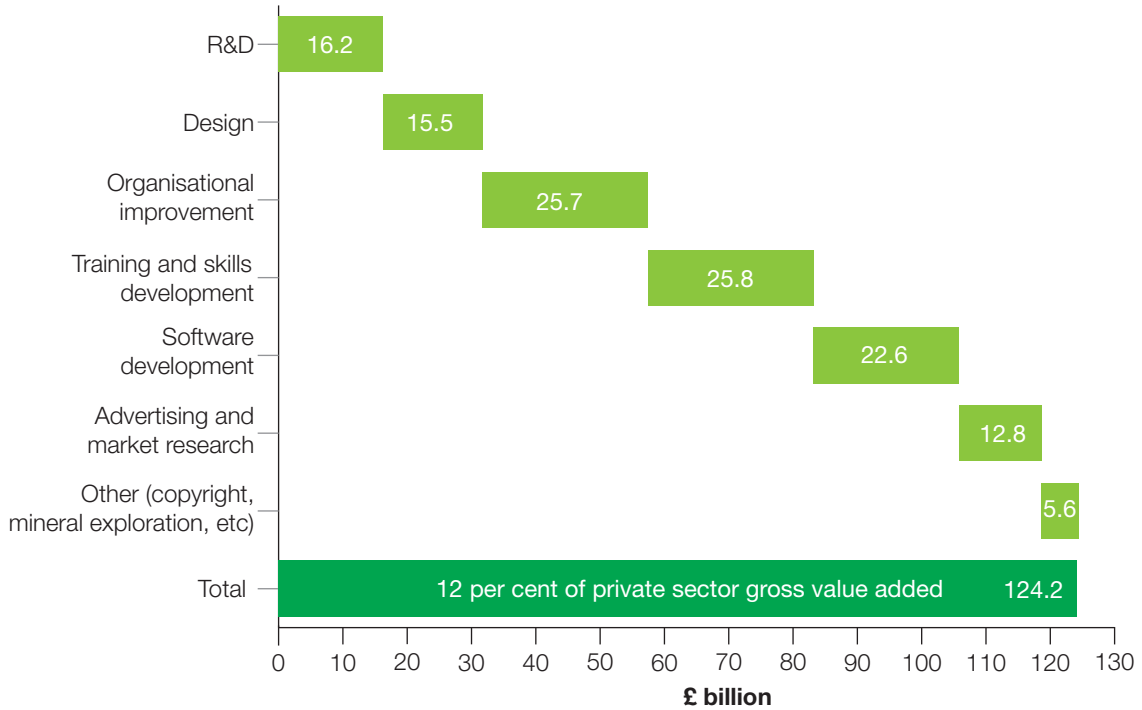
4.35 By contrast, research by NESTA suggests that while investment in traditional innovation – notably R&D, design and copyrighting – in the UK is relatively low, investments in other knowledge assets such as organisation, branding and software has historically been higher than in many other leading economies. Together, investments in these areas of innovation accounted for over 70% of total investment in intangible assets in the UK in 2009 which totalled £124 billion⁵³.

51 BIS, *Innovation & Research Strategy for Growth*, 2011

52 OECD, *Main Science and Technology Indicators*

53 NESTA *Innovation Index* 2012. Note that its uses a wide definition of R&D, which includes scientific R&D (£14 billion), non-scientific R&D (£0.8 billion) and financial products development (£1.5 billion).

Chart 4.2: Investment in intangibles by type, £ billion, 2009



Source: NESTA Innovation Index, 2012

4.36 The Government’s recent Innovation and Research Strategy⁵⁴ seeks to build on our strengths, establishing long term objectives and setting a national framework to support business led innovation and our next generation of innovators. Only by empowering those who really understand the economic opportunities of their own communities will we get the best results for the public support provided. Government support for innovation therefore needs to help better connect this national strategy with local initiative.

Recommendation 41: The Department for Business, Innovation and Skills and the Technology Strategy Board must set out a clear statement explaining how they and other government agencies will work with LEPs and the devolved administrations to better connect national strategy with local initiative.

4.37 We can and should go further – through building on best practice. Some of our universities are world-leaders when it comes to commercialisation of research and engaging with business. All our universities need to learn from them to develop their knowledge transfer activity to the level of the best internationally. Local chambers and trade bodies should actively link their members into their local, or relevant, research base to help them address their innovation challenges.

54 BIS, *Innovation & Research Strategy for Growth*, 2011

4.38 The Department for Business, Innovation and Skills is the custodian of the science and research budget on behalf of the whole of government. Publicly funded research impacts strongly not only on the objectives of the Business Department, but on departments' objectives across the whole of government. The Technology Strategy Board and Research Councils have a unique insight into the research strengths and needs of the country, across a whole gamut of government departments' objectives. As I said in Chapter 3, government departments should ensure they bring this unique perspective to bear in developing each of their individual growth commitments.

Recommendation 42: All government departments, working through the Chief Scientific Advisers Committee, should consult with the Technology Strategy Board and Research Councils UK on the development of their growth commitments.

4.39 Government, as the largest customer in the UK through the goods and services it buys, has a significant opportunity to foster and support innovation through its own suppliers (see Table 4.1).

4.40 When government behaves as an intelligent lead customer engaging with business in pre-commercial stages of product development it can generate more effective and efficient solutions to its own issues. It can also support economic growth, encouraging the development of globally competitive products and services.

4.41 The need to thrive and survive in competitive markets naturally forces businesses to work with their suppliers to seek competitive advantage. Government does not face the same survival imperative and also has to operate within the framework of EU and WTO treaty obligations governing public procurement. This, coupled with complex and bureaucratic processes and a lack of mechanisms for seeking innovative solutions, has traditionally made the public sector a weak lead customer. The UK's performance in encouraging innovation through procurement is poor. We are currently ranked 59th in the world for the government procurement of advanced technology⁵⁵. A number of our key competitors rank significantly higher – Singapore, Finland, the US and Sweden are all in the top 10.

4.42 There are pockets of good work across the Government to address these barriers but they are too small scale and not coordinated effectively enough to have a serious impact as a driver of competitiveness and innovation in the economy. For example, the potential of the SBRI as a tool for solving the toughest challenges in public service delivery and policy remains underexplored in many areas. To raise government's capability to be an intelligent lead customer these initiatives need to be scaled up to achieve maximum impact.

55 World Economic Forum *The Global Competitiveness Report 2011-12*

- 4.43** We also need to ensure that successful innovations developed through public procurement are deployed as widely as possible and that the companies which develop them can use the innovations to grow their customer base. The NHS report, 'Innovation, Health and Wealth'⁵⁶ found that while the NHS is recognised as a world leader in invention, the spread of these inventions within the NHS has often been slow, and too many fail to achieve widespread use.

Small Business Research Initiative (SBRI)

SBRI supports government departments to act as a more intelligent lead customer. It is modelled on the US Small Business Innovation Research programme.

Delivered by the Technology Strategy Board, SBRI is a competitive process for ideas to address specific public sector challenges. The best ideas are selected and typically funded through a two stage process to first prove the feasibility of the idea and then to develop a prototype. The intellectual property rights remain with the company enabling them to maximise the economic benefit of the proposal.

Competitions cover a wide spectrum but have so far predominantly focused on operational effectiveness. For example, the Department of Health has used SBRI to look for better means of detecting pathogens and improving hand hygiene to combat MRSA. The Ministry of Defence (MoD) has sought ideas on how to make a major reduction in the 70kgs that soldiers have to carry into battle. And the Home Office has run competitions to find solutions to reduce mobile phone theft.

The approach can also help to identify and coordinate activity in areas where there will be similar challenges faced by different areas of government. For example, a competition run with the MoD's Centre of Defence Enterprise for battlefield medical technology has helped to develop solutions that can be applied within the health sector in the UK and overseas.

Since April 2009, 1,010 contracts worth a total £88 million have been awarded involving challenges from 35 public sector bodies and departments spanning the breadth of government.

- 4.44** A capability needs to be developed that will help public sector organisations to:
- systematically identify problems that require an innovative response and then collaborate as intelligent lead customers
 - understand how to work with business in order to stimulate, support and shape innovative responses to address unmet needs.

⁵⁶ Department of Health, *Innovation, Health and Wealth, Accelerating Adoption and Diffusion in the NHS*, 2011

Recommendation 43: Rather than setting up duplicate teams across government, a single source of expertise for innovative procurement should be established that builds on existing work and successful mechanisms. This resource should help to aggregate demand and coordinate activity around shared innovation challenges, provide expertise, coordination and guidance, and scale up and develop innovative procurement initiatives.

- 4.45** Once new technologies have been developed and commercialised, we should secure maximum economic benefit in the UK from their onward sale. Standards play a vital role in bringing new ideas to market faster. They are the priceless ingredients that underpin the dissemination of all emerging technologies. They are a form of knowledge – setting out a way forward for new technologies as they are being developed. They define terminology and shape principles and processes for industry to rally round with confidence. As we see in all walks of life, those who set the agenda often enjoy a clear advantage over those who simply follow. So it is with technology – the countries that lead the way developing standards for new innovations enable their businesses to take that first mover advantage onto the international stage.
- 4.46** The UK should exercise leadership in the development of standards that support all areas of technological research, development and innovation to drive growth in UK industry. Delays in defining standards carry a real and significant price as competitive advantage is lost to other countries.

Plastic electronics

Despite the fact that the UK led the world in plastic electronics research through the 1990s and 2000s, this new growth industry was lost to the nation largely because of the failure to rally UK companies around a standardisation strategy for the new technologies. This would have defined an agreed way forward for a UK plastic electronics industry, providing the confidence needed to make large scale investments. Unsurprisingly, the opportunity was grasped elsewhere and the bulk of manufacturing value is now located in Russia and Germany.

- 4.47** Germany is often lauded as the best in the world at standards thus giving German businesses first mover advantage. Germany has strategic goals for standardisation to promote technological convergence, provide efficient tools for industry and be an instrument of deregulation. Support is available to academics in their research programmes to develop a standardisation strategy that will accelerate their route to market.
- 4.48** New standards can only be set through discussion and consensus between those involved in developing, producing and using a new technology. However, all too often all in the UK – innovators, businesses and arms of government – see standards as an after thought, as something that can be bought off the shelf from other countries when a new

product is ready for launch. Even worse, some perceive that standards are a form of government intervention or regulation, creating burdens without adding value. It is said that British innovators too often fear that discussing a new standard with others in their sector will somehow blow the secret of their new invention.

- 4.49** What we need in the UK is not a change to the system for how we set standards, but a change of culture. Early engagement with a future supply chain, end users, customers and government through the standards process is necessary to maximise the benefits of research and innovation for the UK economy. The British Standards Institution, as the UK national standards body, is already engaged with the business community to help all understand the commercial benefit for British businesses of UK leadership in making standards. The Technology Strategy Board and Research Councils play a powerful role supporting innovation and new technologies in the UK. They too need to reinforce at every turn the importance of the UK setting standards if we are to deliver the products of UK research to market faster and with real global competitive advantage.

Recommendation 44: The British Standards Institution, Technology Strategy Board and Research Councils UK should work together to ensure that new standards are set earlier in the development of new technologies in the UK.

Rules of the game

- 4.50** Much of the most visible action by government is in the rules it sets – the laws by which we all live and within which our businesses operate. Much of this comes from central government taking new legislation through parliament. A whole swathe more comes from independent economic regulators set up to ensure markets work effectively.
- 4.51** But in the line of business all of this is wrapped up in the working of officials in regulators and their inspection procedures. To understand the scale of the problem I set out a list of national regulators each of which in its own way has powers to make rules, impose them and monitor their enforcement.
- > Animal Health and Veterinary Laboratories Agency
 - > Animals in Science Regulation Unit
 - > Architects Registration Board
 - > British Hallmarking Council
 - > Care Quality Commission
 - > Charity Commission for England and Wales
 - > Civil Aviation Authority
 - > Claims Management Regulation Unit

- > Coal Authority
- > Companies House
- > Competition Commission
- > Council for Healthcare Regulatory Excellence
- > Drinking Water Inspectorate
- > Driver and Vehicle Licensing Agency
- > Driving Standards Agency
- > Employment Agency Standards Directorate
- > English Heritage
- > Environment Agency
- > Equality and Human Rights Commission
- > Financial Reporting Council
- > Fish Health Inspectorate
- > Food and Environment Research Agency
- > Food Standards Agency
- > Forestry Commission
- > Gambling Commission
- > Gangmasters Licensing Authority
- > Health and Safety Executive
- > HM Revenue and Customs
- > Homes & Communities Agency
- > Information Commissioner's Office
- > Insolvency Service including Insolvency Practitioner Unit
- > Intellectual Property Office
- > Legal Services Board
- > Marine Management Organisations
- > Maritime and Coastguard Agency
- > Medicines and Healthcare Products Regulatory Agency

- > National Measurement Office
- > Natural England
- > Office of Communications
- > Office for Fair Access
- > Office for Standards in Education, Children's Services and Skills
- > Office of Fair Trading
- > OFQUAL
- > Office of Rail Regulation
- > Office of the Regulator of Community Interest Companies
- > OFGEM
- > Pensions Regulator
- > Rural Payments Agency
- > Security Industry Authority
- > Senior Traffic Commissioner
- > Sports Grounds Safety Authority
- > Trinity House Lighthouse Service
- > Vehicle and Operator Services Agency
- > Vehicle Certification Agency
- > Veterinary Medicines Directorate
- > Water Services Regulation Authority

Recommendation 45: The Government should survey the practices and procedures of all regulators involved in conjunction with the sectors affected with a view to simplifying procedures and avoiding unnecessary duplication between agencies.

- 4.52** Ask people how the Government could spur growth in the economy and most will have regulation somewhere towards the very top of the list. That is to say – regulate less.
- 4.53** Many firms cite over regulation as acting like a tax and ask for greater freedom from central control. Yet we need look no further than the economic catastrophe of 2008 to see the problems of under regulation, where excessive risk taking by many banks caused a meltdown so massive that just about every major economy in the world has still to recover.

- 4.54** I reject the premise that regulation in itself hinders growth. Good, well designed regulation can stop the abuse of market power and improve the way markets work to the benefit of business, employees and consumers. A civilised society must provide a clear framework for the behaviour of firms, with boundaries. Some regulations actually create new markets and deliver jobs. For instance, the Motor Cycle Crash Helmet Act of 1973 not only saved lives but created a new market in skid lids that is now thriving. The point is that good regulation strikes a proper balance. When such a balance is reached the most powerful result is seen – growth.
- 4.55** To find this balance, government must have a continuous dialogue with industry to ensure all regulations deliver on this growth ambition.
- 4.56** When I was President of the Board of Trade and in charge of the deregulation initiatives of the time, I invited trade associations to submit to me the changes they would make to existing regulations. I asked for the exact wording and promised I would investigate each and every submission personally. At the end of the deadline I had received no submissions. Not a single one. Telling this story during this review, many bodies have promised me that they would be more than happy to take me up on the offer again.
- 4.57** It is no good continuing to have a general debate between government and the business community about the effectiveness of regulation. We need clarity about where regulations are impeding growth, and if so, whether they are nevertheless necessary or proportionate. The Government should therefore again write to trade bodies setting out clearly the body of regulations affecting their members and asking the sector to state precisely what further changes it would like to see made and why, speaking now or forever holding their peace.
- 4.58** The creation, revision and removal of regulations should be a clear collaborative exercise between government, the private sector and other interested parties. The Red Tape Challenge⁵⁷ demonstrates the power of such collaboration. In some areas – notably immigration, to which I will return later – it needs to go much further. It also needs to be done quickly. Having spent 18 months reviewing its first 24 themes and agreeing and announcing changes to over 1,100 regulations, the changes now need to be delivered with minimal delay. All departments should set out their timetable for implementing the agreed changes before the end of this year.

Recommendation 46: Government should involve the private sector in drafting regulations so it is a collaborative process. It should invite trade associations, through the lead associations for their sectors, to submit precise redrafting of existing regulations prior to wider consultation on any changes.

- 4.59** Having clarified the private sector’s position on existing regulations, this collaboration should extend to working together on any future regulatory changes.

57 <http://www.redtapechallenge.cabinetoffice.gov.uk/home/index>

4.60 Many manifestations of regulation are devolved to an army of quangos. Some – particularly the economic regulators – are set up with the very purpose of making markets work more effectively, intrinsically supporting growth. Many others among the non-economic regulators are not required to have regard to the impact of their regulatory activities on our economic prospects. I would not wish to turn the clock back to having ministers make every regulatory decision. But I do want to stress the importance of regulators understanding and taking proper account of the economic consequences of their decisions. Government must find a way to ensure that this happens.

Recommendation 47: Through its review of both the Principles of Economic Regulation and the Compliance Code for non-economic regulators, the Government should impose an obligation on regulators to take proper account of the economic consequences of their actions.

4.61 Every high-performing organisation undertakes regular reviews of its strengths and weaknesses. This is even more important for arms of government given their powers over third parties. Regulators, as with all quangos, are subject to triennial reviews. Yet as it stands there is no formal requirement for those who are on the receiving end of the regulator's actions to be heard. Listening to these interested parties, alongside others, could lead to improvements in both the quality of regulations and how they are enforced.

Recommendation 48: In preparing for any review process, regulators should invite the lead sectoral trade association (or a national body in the case of horizontal regulators) to analyse and publish evidence on the impact of the regulator's activities – both what it does and how it does it – on the businesses affected. This published evidence would then be available for analysis and comment by other interested parties.

4.62 As we all hear time and again there is a real cost – direct and indirect – of regulation. The direct costs are recovered from those regulated. While this is an important means of limiting public expenditure, it has the unintended consequence of removing a natural cap on regulatory activity. It is for individual regulators, guided by their sponsor departments, to set their charging policies. However, it is important that in areas of joint authority, such as those overseen by the Environment Agency and Health & Safety Executive together, the policies should be consistent. In common with similar private sector regimes, the policies should also set out basic service standards, such as turning up on time or providing sufficient notice of cancellations.

Recommendation 49: Regulators should set out their service standards and cost recovery policies clearly, showing how much they will charge under what circumstances.

4.63 Human judgement will always contain a degree of variation but it is absurd that two inspectors looking at the same paperwork on two different days can reach two completely different conclusions.

4.64 The reasons for this are manifold:

- > poor training
- > ambiguous guidelines
- > lack of performance management
- > poor auditing
- > poor accountability for decisions.

4.65 But whatever the reasons, it is the responsibility of regulators to understand and address them. This is happening in some cases already – the Better Regulation Delivery Office has set up the Primary Authority scheme, in which local authorities work together to improve consistency in their regulatory areas (trading standards and environmental health). This should be the norm.

Recommendation 50: Regulators should publish policy statements showing how they will ensure that their decisions are both internally consistent across their geographic area, and consistent with those of any other bodies which regulate the same businesses.

4.66 Following the 2005 Hampton Review⁵⁸, many regulators already practice some form of earned recognition – exempting reliable and compliant businesses from further inspection or other burdens for a given period after reaching a certain standard. This makes sense and any regulator that does not already practice it should work out how to introduce it. But too often changes of policy or personnel at regulators cause them to restart inspecting these compliant businesses, increasing burdens and cost. The regulators should meet the costs of these regulator-led changes, not the compliant businesses.

Recommendations 51: All regulators should adopt systems of earned recognition and meet the cost of inspections carried out at the discretion of the regulator within any recognition period.

4.67 Finally, every regulator should acknowledge that it is not always right. Often a business will not complain or criticise for fear of alienating its regulator, though the decision may be questionable. A business which seeks legal advice can end up in the absurd position of paying both its own lawyer and the regulator to argue with each other. In many cases the person to whom the challenge is made is the line manager of the official who made the original decision. This is clearly not a sensible way to approach the issue. Businesses should be able to seek an unbiased second opinion without fear of cost or reprisals.

58 <http://www.bis.gov.uk/files/file22988.pdf>

4.68 I do not intend to open the floodgates to rogue businesses gaming the system – there must of course be legitimate grounds for seeking a second opinion. But it is up to regulators, as part of their duty to their customers and partners, to demonstrate that this process is genuinely independent, transparent and quick.

Recommendation 52: All non-economic regulators should publish policies showing how their customers can ask, without prejudice, for an independent second opinion on a regulatory decision or requirement.

4.69 Much of the body of regulation in the UK is conceived in Brussels. Ensuring that such regulation works to the best interests of the British economy is the responsibility of the Government. The current work of the Foreign Secretary in this area is to be commended. Departments are being asked to provide details on EU business within their responsibilities and the Foreign Office is taking a strategic role making sure government activity in Europe is proactive, joined up and produces the desired outcomes.

4.70 The Foreign Secretary and his ministerial team alone cannot fight our cause in Brussels. Our European neighbours do not leave it to one department – their cabinet members are in Europe on a regular basis putting their causes forward. We need to make sure our secretaries of state are there too – and that they are combining forces with our business representatives who devote considerable resource already to arguing the UK's case in Brussels.

4.71 It also goes beyond cabinet level. In 2011, the then Parliamentary Under Secretary of State for Employment Relations, Consumer and Postal Affairs, looking to improve the quality and impact of conversations he was having in Brussels, instigated the Likeminded Group on EU Growth. Bringing together ministers from 16 Member States, the group has met several times to discuss areas of mutual interest and agree shared outcomes to the benefit of all member states. This proactive approach to European relations is to be commended and is an exemplar ministers at all levels should follow.

Recommendation 53: The Government must continue to promote the British interest in Europe and all secretaries of state with EU business affecting their department should make bi-annual trips to Brussels to influence decision making throughout the EU policy making process. All departmental ministers with EU business should consider every proactive step possible to put Britain on the front foot at the negotiating table.

4.72 To complement the Foreign Secretary's work, departments could and should do more to identify at an early stage EU business that affects them, and work out how to influence it.

4.73 The work of the Department for Transport (DfT) has been commended as an exemplar of what other departments ought to be doing. At the DfT, potential new EU regulations are identified up to two years in advance. This enables the department to influence EU institutions and other Member States before the policy becomes set in stone.

EU policy at the Department for Transport

With much of the Department for Transport's (DfT) regulation coming from Brussels, the Department is committed to stepping up its engagement with the EU institutions and other Member States. Central to DfT's strategy is engaging early with EU proposals for legislation. Getting involved *before* the European Commission formally publishes legislation maximises the chances of influencing EU policy in the UK's favour. This means the Department should be better placed to halt regulations which impose unnecessary burdens on UK business.

In practice, DfT scans for upcoming EU regulation. An important source for this upstream intelligence is the Commission's Work Programme which, similar to the Queen's Speech here, sets out the legislative agenda for the following 12 to 18 months. DfT also encourages businesses to get in touch if they have concerns about upcoming EU regulation. Findings are then subjected to an internal challenge process to test potential regulatory impacts at an early stage. This scrutiny helps set the Department's EU engagement priorities, ensuring that resources are focused on minimising potential EU regulatory burdens.

- 4.74** This combination of early identification, internal challenge, cabinet level engagement and Foreign Office coordination is the mix needed to ensure that Britain is in the best possible position to shape the development of EU regulation.

Recommendation 54: Government departments should develop greater capacity to identify forthcoming EU regulations well in advance.

Planning

- 4.75** There is one area of regulation which is at the top of the growth agenda – planning. Planning decisions are key to unlocking the infrastructure that we need for growth.
- 4.76** I remember arriving as a fresh faced cabinet minister in 1979 at the Department for the Environment and asking to see the rules placed on local authority housing developments. I was shown the forms, asking no fewer than 80 questions, including slope of the roof, colour and type of brick and window area. I used to keep the forms pinned up on my wall to remind me of the perils of over regulation. On the other hand, left to their own devices a few private sector house builders would construct houses of unacceptable quality without the building regulation regime. I therefore strongly support the purpose of the 1947 Town and Country Planning Act to bring order to our planning system.

- 4.77** However, planning decisions are still too often lengthy and bureaucratic. There is simply no sense of urgency or any understanding of the economic cost of delays. The appeals system adds more time to the process. Nowhere else can the pedestrian speed of decision making in this country – and its effects – be more damaging than in planning. There are countless jobs tied up in the filing cabinets of the planning machine.
- 4.78** To be clear, I am not calling for the nature of those decisions to change. I support fully the rights of interested parties on both sides of any decision to have their views taken into account. The outcome just needs to be reached more quickly. I believe that the Government is moving in the right direction on this issue, but I think more can be done.
- 4.79** When decisions are taken, applicants are often reluctant to appeal to the Planning Inspectorate, especially if they do a lot of business with their planning authority. The Inspectorate should be given powers to call in any application after six months which they consider is being dealt with inefficiently, to ensure that decisions are reached with optimum speed.
- 4.80** With the exception of massive and complex projects – for which the Government has introduced a separate process precisely to speed things up – most planning applications do not involve very many contentious issues. These are usually known well in advance, and almost all come to light as soon as the application is published for consultation. For any application still undecided after three months, the planning authority should publish a clear and unbiased statement of what the issues are. This will help all parties to understand what is standing in the way of a decision. It will have the positive effect of galvanising both planning authorities and statutory consultees, to ensure that the issues are fully explained within three months.
- 4.81** It should not take longer than three months to reach conclusions on the issues. So any application still undecided after six months should automatically go before the Planning Inspectorate.
- 4.82** The appeals process should be speeded up along the same lines – issues known and articulated after three months, decision after no more than six months.
- 4.83** I believe the most likely effect of these proposals is that faced with the possible intervention of the Inspectorate, local planners will simply do the job they are paid to do more quickly. Everybody has to play their part in speeding it up – applicants, councils and consultees.

Recommendation 55: The Planning Inspectorate should be given powers to investigate planning decisions proactively. The Government should also consider on a rolling basis all the possible options to inject urgency and purpose into the planning system.

- 4.84** There is a marked difference in the responsiveness and quality of advice from private and public sector players in the planning system. If advice is sought from a private firm of consultants, a senior partner arrives within days and immediately indicates what will and will not be possible. The local authority similarly consulted will often send a junior official who caveats everything they say with the fact that they are not empowered to make any decisions and warns that their advice might be incorrect or overruled.
- 4.85** As with all activities of government, work should be undertaken where it can be done most efficiently and effectively. The Government has recently consulted on proposals to bring more private sector expertise into listed building consent applications. My suggestion is that this would work best as a dual key system – government could issue licences to private firms competent to make decisions on, for example, alterations to listed buildings, and licences to trusted owners to use those private firms to decide their applications. English Heritage would retain call in powers. This could remove a massive blockage from the local authority system and free up planning resources to speed up other cases. The private firms would ensure that their decisions were in line with the legislation, and the applicants would refrain from abusing their position, for fear of losing their licences.
- 4.86** The Government uses Local Development Orders (LDOs) as mechanisms for allowing development to take place in specified areas without the need for an individual planning application. Three LDOs have been adopted so far.
- Hertsmere Borough Council aims to help regenerate Borehamwood town centre and assist in the success of the television and film industry by allowing certain changes of use and minor development.
 - Wycombe District Council is currently consulting on a policy to allow changes of use to properties in the town centre in order to encourage use of vacant properties, assisting in the regeneration of a key historic quarter of the town centre.
 - Minor works to the public realm and specified change of use of properties would be permitted in a central area of Swindon with the aim of encouraging use of vacant properties and facilitating improvements to the public built environment.
- 4.87** In practice the application of LDOs seems to have been restricted in their use to relatively minor schemes.

Recommendation 56: The Government should consider the effectiveness of Local Development Orders and extend their use after consultation with affected parties to establish best practice.

- 4.88** Another planning tool available to the Government is Special Development Orders (SDOs). My own experience with SDOs is one of mixed fortune. In the early 1980s in order to revive architectural competitions I reached agreement with Ronnie Lyon, a property developer, that if he could acquire two sites, one on either side of Vauxhall Bridge on the

south bank of the Thames and conduct an international architectural competition to achieve the highest standards for this important gateway, I would ask Parliament to expedite planning permission via the SDO legislation. Events proceeded as we have agreed, proving the process could work within very short timescales. Sadly Ronnie Lyon was declared bankrupt before a brick was laid.

- 4.89** However, there are many examples of the successful use of SDOs. For example, an SDO was created for the Bristol Urban Development Area in 1989 to allow the Bristol Development Corporation to develop parts of the east of the city.

Recommendation 57: The Government should consider using Special Development Orders to speed up specific planning decisions of strategic significance.

Special Development Orders

Special Development Orders (SDOs) enable Parliament via secondary legislation to accelerate the normal planning process. Each SDO is a statutory instrument subject to the negative resolution parliamentary procedure.

Around 19 SDOs have been made, most in the 1980s, to allow the Government to approve large scale development within specially defined areas, with Urban Development Corporations managing the development process.

- 4.90** Alongside inefficiencies in the planning system, derelict and unused properties are a major drag on our local economies. It is important that we make the most of all public property holdings, both central and local government owned. Surplus and derelict land should not be wasted. The Government Property Unit was set up in 2010 to support central government departments in rationalising their use of property assets. As part of this they use a database, ePIMS. This records properties, land, along with declared surplus land, buildings and vacant space for all central government holdings, as well as for some local authorities. It is curious that this initiative was preceded by the establishment of the Land Registers, designed exactly for this purpose. Why this initiative fell from use is lost in the mists of time.

- 4.91** ePIMS should now be made comprehensive so that it can provide a complete picture of all public land holdings. LEPs and local authorities would then be able to identify surplus public land and properties in their areas that they could support being brought back into productive use as part of their local economic strategy.

Recommendation 58: The Government Property Unit should work with local authorities to identify and publish details of all surplus and derelict public land on the ePIMS database so that LEPs and local authorities can collaborate to bring this land back into reuse in support of the local economic strategy.

- 4.92** As well as looking at public land holdings, LEPs should consider what they can do to encourage the regeneration of disused private land holdings as part of their economic strategies.

Capacity in the economy

- 4.93** Central government has a fundamental responsibility to create the national economic capacity upon which local growth relies: the national infrastructure – transport, energy and those rare but vital nationally-transformative regeneration projects – which enables the country to function effectively. Alongside my proposals for devolving authority for local infrastructure, central government must retain control of important, large scale infrastructure projects. This includes our motorway network, national rail network and airports, as well as our energy networks. National and regional interconnectivity is critical to our future prosperity. The Government must have a clear long term plan that sets out how our future large scale infrastructure investments will meet the needs of business to deliver growth.
- 4.94** The Treasury’s Infrastructure Plans⁵⁹ identify many nationally significant projects that require central coordination. It backs these up with spending commitments and government support. These projects are vital. We have seen this in successes of the past – the Channel Tunnel and High Speed 1 (HS1), the Dartford crossings and the London Docklands Development Corporation – that have unlocked growth. Indeed, we need look no further than the extraordinary events in London 2012 just a few months ago for evidence of the power of large scale investments.

High Speed 1

In the 1990s, I intervened decisively to ensure HS1 was constructed via the Arup route through east Kent and the Thames Gateway. A serious part of my argument was that this would enable the regeneration of Stratford. It seems to me extraordinary that, with such an enormous opportunity, HS1 was sold to overseas investors without any requirement to stop at a station that had already been built. I do not believe that decisions of this sort can be taken purely on the basis of the short term capital proceeds of a sale.

- 4.95** With the memories of the Olympics and Paralympics still fresh in our minds, I am delighted the Government signalled the ongoing importance of these major infrastructure projects with the appointment of LOCOG’s Paul Deighton to oversee delivery of its infrastructure plans. His track record is formidable. I hope it is a clear sign that governments will, in future, continue to seek private sector expertise within their ministerial ranks.

⁵⁹ HM Treasury, *National Infrastructure plan*, 2011, http://www.hm-treasury.gov.uk/national_infrastructure_plan2011.htm

Major infrastructure decisions

4.96 Responsibility for large scale infrastructure projects must remain at a national level as the implications of such schemes – and the costs of their implementation – go beyond any one local area. There are a number of tough decisions facing government on such projects that could unlock multi billion pound investment. These projects are crucial to our future competitiveness – the market urgently needs certainty in order to bring this private investment on stream. Let me take two examples.

Thames Gateway

4.97 The as yet unexploited opportunities in the corridor of the Thames stretching from East London out eastwards, past south Essex and north Kent, make it probably this country's greatest single prospective area for growth.

4.98 The history of urban regeneration tells us of the extraordinary results that can be achieved when the public and private sectors come together to deliver a shared vision for growth. In 1981, we established the London Docklands Development Corporation (LDDC), to help revive the fortunes of London's East End area.

4.99 The LDDC was a joint venture between the public and private sectors and was the most ambitious of all the Development Corporations. The London Docklands area had seen over two decades of rapid decline, as the docks moved downstream to the deeper water needed for large container ships, and the utilities relocated. The LDDC not only brought the public and private sectors together, it also had key powers such as land acquisition, planning and Geoffrey Howe's concept of enterprise zone status. The LDDC's approach to decision making, identifying the strengths and possible growth opportunities in the widely derelict area is an exemplar for local growth plans to be published by LEPs.

- > The Docklands' location near to the City of London made it an excellent place for the banking and finance sectors to locate more of their staff, especially given the lack of space in the City. What you see now is Canary Wharf and the massive developments around it.
- > It inherited miles of disused railway lines and so created the Docklands Light Railway which, 30 years on, is growing every year.
- > It spotted the massive growth in aviation and identified a prime site of disused land on which the private sector could build London's most centrally located airport – London City.
- > It identified a large site north of the river and mapped it to the gap in the market for a large conference centre in London, thus enabling the creation of the Excel Exhibition Centre.

- 4.100** The legacy of the LDDC is there for all to see and enjoy, and London's Docklands continues to expand. The O2 has now become the world's most visited entertainment venue. Both it and the Excel played host to the London Olympics and Paralympics this year, welcoming the world's athletes and sports fan to the once derelict area. Also this year, the Emirates Air Line – a new £60 million public-private sector investment – opened up between the two sites. If in 1981 you had told the leaders of Greenwich and Newham Councils that their two boroughs would one day be joined by a cable car, they would have laughed at you.
- 4.101** Urban development on a large scale is usually undertaken by central government. Such a process needs to harness and enthuse the strengths of the public and private sectors in support of a vision backed by a delivery vehicle.
- 4.102** Existing arrangements for the development of the Thames Gateway are wholly inadequate. The current membership of the Thames Gateway Strategic Group – the body taking forward the future vision for the area – includes the Parliamentary Under Secretary of State at the Department of Communities and Local Government and one representative from each of the Greater London Authority, Swale Borough Council, Gravesham Borough Council, Kent County Council, Castle Point District Council, Medway Council, Southend-on-Sea Borough Council, the London Borough of Greenwich, Thurrock Council, Dartford Borough Council, Essex County Council, the London Borough of Newham, the London Borough of Havering, the South East LEP and the Thames Gateway Kent Partnership.
- 4.103** These arrangements will just not do. You cannot have a serious discussion about the future of this hugely important part of our country with just two business voices at the table. The arrangements need to be brought more into line with the approach of the LDDC and be a proper collaboration between central and local government and the business community. The leadership needs to be someone with excellent private sector credentials and experience.

Recommendation 59: The Government should set up a new Development Corporation under an independent chairman from the private sector, comprised of representatives of central government, the Mayor of London, London boroughs, Kent and Essex councils and with a majority of members from the private sector and related disciplines. It should not exceed 20 members. Once created the Corporation should be given the powers it needs to drive its vision for future growth. It should be able to bid for its funds from the single pot.

- 4.104** It is important to avoid planning blight to the maximum extent possible. An early responsibility of a new development corporation should be to release the vast proportion of the area covered from its planning disciplines so that local authorities' responsibilities remain intact therein.

- 4.105** These proposals are in practice a limited qualification of the very localist agenda to which the Government is committed. This is designed to raise the ambitions for the scale and quality of development beyond that traditionally associated with a purely localist agenda. It is government kickstarting the process if the local building blocks do not appear to exist.

Airport capacity in the South East

- 4.106** Another critical question is airport capacity. The DfT predicts that, with no new runways, Heathrow, Stansted and Gatwick will be at full capacity by 2030⁶⁰. By 2050, these forecasts anticipate that each year, 42 million passengers from London and the South East will have to use airports outside of the region. Alternatively, of course, people may choose to stay away from London and the South East as other European capitals become easier to use.
- 4.107** These issues are very controversial, and therefore difficult, decisions for the Government to resolve. But the problem will not go away. The Government has asked Sir Howard Davies to chair a commission to investigate the issue and make recommendations as to the best way forward, which I welcome. However, I think the Government should revisit the timing of his findings. He is not scheduled to make his final recommendations until after the next general election in 2015.
- 4.108** I understand the commitments made in the Coalition Agreement to scrap plans for a third runway at Heathrow and the earlier election pledge. However, I believe there is a way forward which injects more urgency into the decision making process – and therefore confidence for all those we want to invest in our economy – without compromising the commitments made.
- 4.109** First, as soon as is practicable, the Government should publish all the options and all the arguments for airport expansion. There will not be any surprises – all the arguments are known and have been very widely debated.
- 4.110** I am not in a position to influence the decision to a particular outcome and certainly would not wish to second guess Sir Howard Davies. But he should be asked to analyse all of these options and provide his advice in the next year, at which point the Government should set out its preference. All political parties could set out their positions in their next manifestos. In the meantime preparatory work could commence, with a commitment that no construction contracts would be let until a mandate had been secured at the next general election.
- 4.111** This would help unblock the current situation, where business sees at least three years more inertia before any indication of direction is provided. A commitment this time next year to a preferred solution would at least provide the private sector, here and abroad, with the necessary confidence that this government has a clear vision for the future.

60 DfT, *UK aviation forecasts*, 2011, <http://www.dft.gov.uk/publications/uk-aviation-forecasts-2011/>

4.112 The politics are uncomfortable. I know from my experience of trying to develop Maplin Airport in the 1970s. But against the current background it will not be possible for the Government to claim credibly at the next election that it has not made a decision or reached a preference about a third runway at Heathrow. Having given so absolute a commitment at the last election, any qualification of such a commitment at the next will be taken as a positive indication. It seems to me better to face the dilemma sooner rather than later with the benefits to business confidence that would follow.

Recommendation 60: The Government should accept the need to clarify urgently its preferred solution to the problem of airport capacity in the South East and indicate that preference whilst making its implementation conditional on the outcome of the next election.

4.113 These are not the only examples of major infrastructure issues that need firm decisions by government – the regeneration of the Atlantic Gateway to make best use of the complementary economic weight of the Liverpool and Manchester city regions is another. These decisions should be taken urgently as part of our determination to be seen as an attractive place to invest.

Energy

4.114 Alongside physical infrastructure, the Government should ensure the UK has the energy infrastructure and capacity to support our future economic growth. As recently as three years ago, it was predicted that the lights would have gone out by now as energy suppliers struggled to meet the needs of the country. This proved a false prophecy as our gas supplies continued and the economic crisis reduced demand. This has not, however, avoided the problem. It has simply delayed it.

4.115 It goes without saying that a secure and affordable supply of energy is essential to everything we do. It also provides opportunities for growth. During a trip to the Humber I heard from everyone I met the importance to the region of investment in offshore wind. Similarly the Severn Barrage offers the possibility of both a long term source of energy and extraordinary economic regeneration.

4.116 It is widely accepted that over the next 10 to 15 years up to £200 billion of investment may be needed to meet both levels of demand for energy and our carbon targets⁶¹.

4.117 For the country's energy needs to be met, the Government needs a clear and consistent long term energy policy that indicates what our projected needs will be and how they will be met, by when and by whom.

61 OFGEM, *Project Discovery Energy Market Scenarios*, 2009, http://www.ofgem.gov.uk/Markets/WhIMkts/monitoring-energy-security/Discovery/Documents1/Discovery_Scenarios_ConDoc_FINAL.pdf

4.118 We have relied in the UK for many decades on private sector funding for our energy infrastructure – nothing I say changes that. But investment planning periods in the energy industry are particularly long. Without real certainty about the UK’s long term energy policy, private investors simply will not risk the enormous sums of capital required to build our energy infrastructure. These problems will not go away. Just as with major infrastructure projects, clear decisions are needed now.

Recommendation 61: The Government needs to set out a definitive and unambiguous energy policy, including the supporting financial regime, to give the sector the certainty to invest.

Funding infrastructure investment

4.119 In the last Budget the Chancellor emphasised the Government’s wish to encourage investment from British pension funds in British infrastructure and explained that the Government was working with a dozen of the largest schemes specifically on that.

4.120 It is impossible to overstate the potential of this work. There is a well of money looking for a better return than currently available in the market or only available in higher yielding equities with attendant risk. In view of the exceptionally low yields currently available, there is a one off opportunity now to match the needs of pension funds with the urgent need to boost investment in the UK’s key infrastructure.

4.121 It is estimated that the UK requires over £250 billion of infrastructure investment over the next five years, the vast majority of which will need to be provided by the private sector.

4.122 Pension funds are potentially a major source of capital for this investment. The scale of assets held by the UK’s pension funds and other investment schemes is enormous. Combined, public and private sector pension schemes have approximately £2 trillion in assets.

4.123 If structured correctly, infrastructure should be a good match for pension funds and long term insurers, providing a source of stable, inflation-linked, longer term yields. However, the current investment model and structure of most UK pension funds does not support efficient investment in this asset class. They are relatively small and need advice and support to understand and invest in infrastructure. The challenge is to ensure that domestic infrastructure schemes are constructed in such a way as to offer funds the security and efficiency they properly require. They need to offer returns that are attractive and accessible to the stewards of long term savings.

4.124 The current procurement process for public infrastructure is time consuming and complex. Few pension funds, except for the largest, have the expertise or time to dedicate to it. The cost of the investment process is also relatively high for pension funds and insurers who wish to provide finance to these projects.

- 4.125** The current procurement model requires a one-size fits all funding solution for the life of the project. The two stage nature of most infrastructure projects would benefit from a different approach – there is a higher risk construction phase, typically two to four years, which would be best suited to experienced banks. The second 20 to 30 year operational phase, which should have lower risk, could be well suited to pension funds. Whilst historically this has been undertaken by banks, the procurement process needs to be reviewed to reflect the needs of long term investors.
- 4.126** As a result of the Government's initiative, action is being taken to address some of these deficiencies. The National Association of Pension Funds and the Pension Protection Fund are in the process of raising initial development capital to establish a £2 billion Pension Infrastructure Platform to allow pension funds to invest directly in UK infrastructure assets. This is designed to overcome the problem that many funds are too small to be able to afford the due diligence necessary to analyse often complex infrastructure investment offers.
- 4.127** Pension funds are rightly conservative by nature and are hesitant to accept new types of investment. Structures and processes need to be absolutely right in order for them to participate. The Government's Infrastructure Guarantee Scheme announced in July this year should help here, effectively improving the asset class of infrastructure investments by reducing the attendant risks.
- 4.128** Insurers are the other potential pool of long term capital for infrastructure investment. They are larger, move faster, and are more able to bear the costs and complexity associated with domestic infrastructure investment. However, after years of being crowded out by banks lending in this space, they need to build up the teams and processes to be able to participate. The banks, which are still driving the funding of infrastructure projects, are currently not incentivised to change or advise their clients on alternative sources of finance. We need to develop a model that allows them to use their expertise profitably on these projects and create an investable product for longer term providers of capital.
- 4.129** Although the need is clear and urgent, progress since last December has not matched the Chancellor's ambition. The issues are complex and nothing should be permitted to obscure the fiduciary responsibilities of the funds. That said, traditional attitudes may be holding back progress and existing negotiations might benefit from an injection of urgency and external support.

Recommendation 62: The Government should initiate discussions through the Bank of England and, in cooperation with the appropriate regulators, seek one or more solutions to enable UK pension funds to invest in UK infrastructure assets. The Government should ensure that best practice applies to both public and private sector pension fund investments.

NO STONE UNTURNED in pursuit of
GROWTH

Chapter 5:

Broadening the capacity for excellence

- 5.1** The UK is home to some of the best companies in the world. They are out there winning every day. Amongst the corporate giants, we have companies such as Rolls-Royce, and GSK, acknowledged leaders in their field, competing on the world stage. At the mid-size level, again, we have some of the most dynamic companies in Europe. The proportion of our mid-size businesses achieving revenue growth of at least 10% a year is ahead of France and Italy, and on a par with that in Germany⁶². There are growth champions too amongst small and medium-sized businesses. A recent report found that around 4.5% of these businesses had achieved high levels of growth over the last decade⁶³.
- 5.2** We have undoubted strengths, with a select cohort of businesses of all sizes already out in front and excelling. They show what UK businesses are capable of achieving. We cannot afford, though, to be dazzled by their success and ignore the performance of the average. To put it bluntly, the performance of the best needs to be extended more widely. We are not, as a nation, as competitive as we need to be to retain our place in the world.

UK weaknesses

- 5.3** Some of our weaknesses are long standing and well-rehearsed. As Chapter 1 described, there have been improvements in UK productivity relative to other G7 countries over the last 20 years. However, UK output per hour worked in 2010 was still 24% behind the US, 19% behind Germany and 18% behind France. We are outperformed in most sectors, but particularly in manufacturing.
- 5.4** Exports are a useful benchmark of international competitiveness in the traded sectors. Here, the UK's share of global export markets has declined over the last 30 years. We are not alone in this. It is part of a trend shared by many other advanced economies. Yet there are signs that our businesses could do better. Only one in five of our SMEs export⁶⁴. This compares unfavourably to SMEs in the rest of Europe where, on average, one in four are exporters. These export weaknesses extend to larger mid-size businesses. The Government's 2011 growth review⁶⁵ of mid-size businesses found, perhaps surprisingly, that there are proportionately more high intensity SME exporters than there are high intensity mid-size exporters.
- 5.5** What is worrying is that many SMEs appear to have an accidental approach to exporting, rather than a strategic plan. In a survey of businesses by the British Chambers of Commerce (BCC)⁶⁶, 58% cited being approached by a customer as a reason for exporting, rather than pro-actively choosing to export.

62 S. Roper and A. Malsche, *Leading From The Middle*, GE Capital, 2012

63 Defined as growth in turnover, profit or employment of more than 20% a year for at least three years. *Breakthrough Growth Champions report*, Santander/Eperian, 2012

64 BIS, *Small Business Survey*, 2010

65 BIS, *Mid-Sized businesses*, 2011, 'Mid-size' in this context is businesses with turnovers between £25 million and £500 million. A 'high intensity exporter' is a business where exports make up over 75% of turnover. www.bis.gov.uk/analysis/statistics/mid-sized-businesses

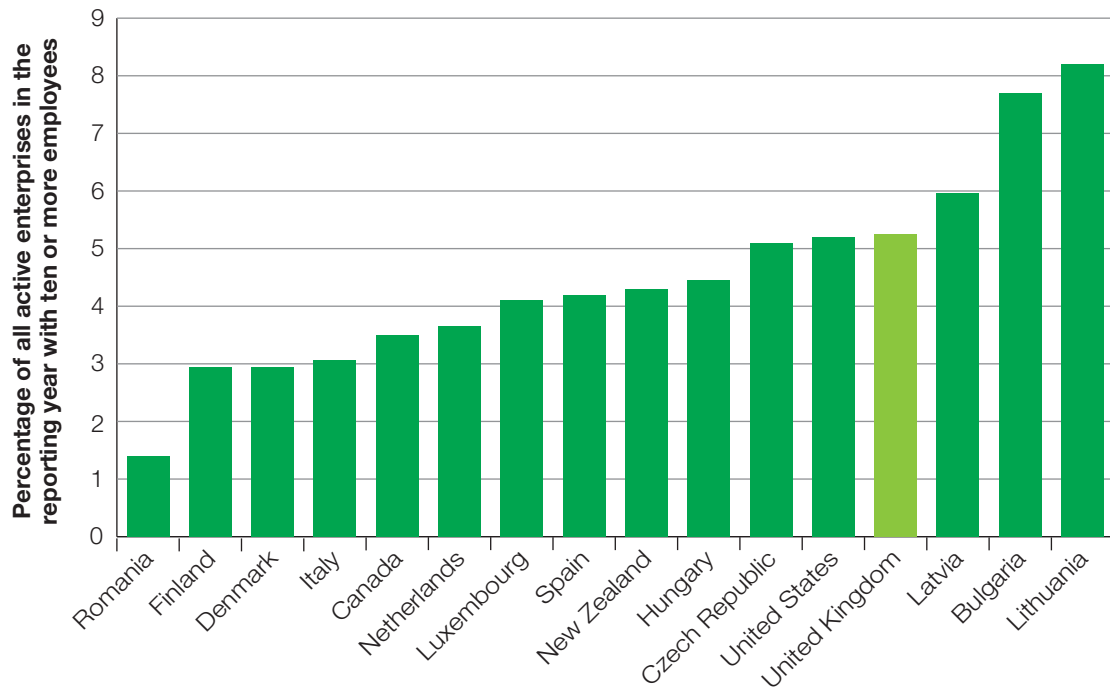
66 BCC, *Manufacturing for export: make or break for the British economy*, 2011

5.6 One of the UK’s strengths is our buoyant start up sector. Start up activity has remained resilient throughout the recent economic crisis, and the proportion of our working age population engaged in starting or running a business stands at 7.6%⁶⁷, well ahead of France and Germany. The number of private sector enterprises in the UK has increased in each of the last 11 years. We are good at creating businesses. What we are less good at, however, is improving business performance in terms of growth and productivity.

The UK has a high proportion of static and negative growth companies

5.7 Recent analysis by NESTA⁶⁸ on growth dynamics amongst businesses in Europe and the US supports the picture of the UK as a country with a small cohort of highly successful businesses. Indeed, amongst the G7 countries included in the report, the UK ranks higher than Italy and Canada and is on a par with the US in terms of its share of firms achieving average employment growth of 20% or more a year over a three year period.

Chart 5.1: Share of high-growth firms in selected OECD countries (2005) – employee-based measure, NESTA



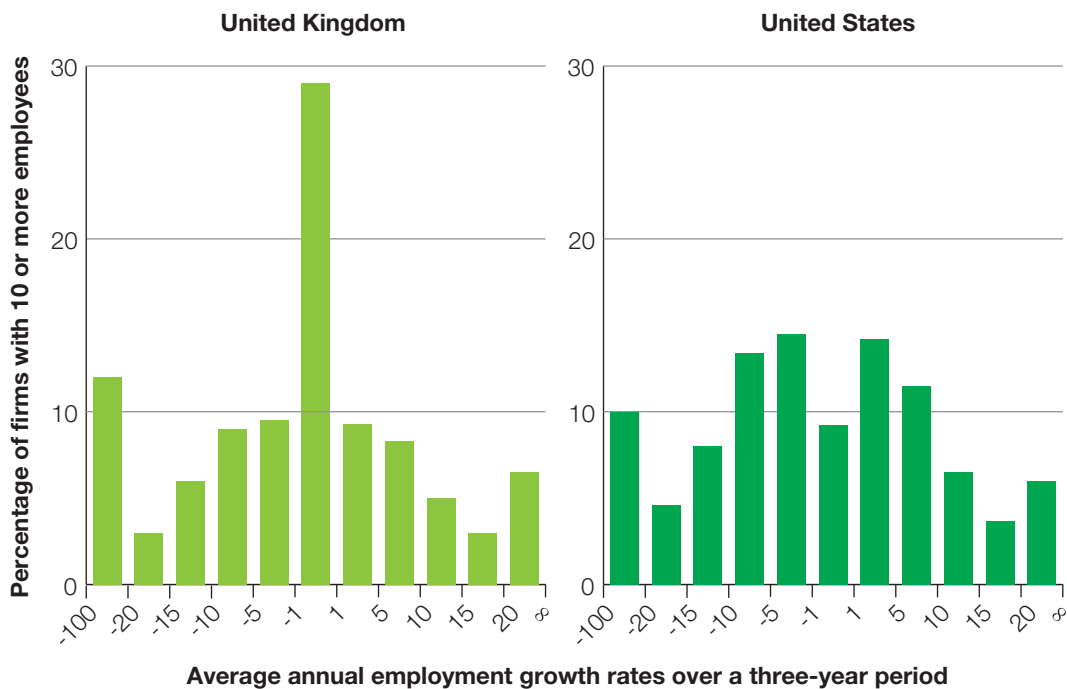
Source: ONS Business Structure Database; OECD Business Demography Statistics

67 Global Entrepreneurship Monitor, UK report 2011, p4

68 Nesta, *The vital six per cent*, October 2009

5.8 We do, however, have a substantial middle of firms experiencing static or near static growth. Chart 5.2 shows that 29% of UK businesses experienced static or very low growth or shrinkage in employment (-1% to +1%) over a three year period. The extremity of the spike is, in part, a result of the banding used to define the distribution. However, even a widening of the central band still shows the UK as having a significantly higher proportion of static or near static businesses than the US.

Chart 5.2: Comparative growth dynamics in UK and US businesses (employment)



Source: NESTA⁶⁹

5.9 These particular charts focus on growth in terms of employment. Growth in output, turnover and profitability are other important measures. It is also crucial that we focus on how productively we use labour and other resources. Only if we continue to raise productivity will we improve our competitiveness, grow our output and create additional employment opportunities.

5.10 The prize is potentially huge. There are about 3.6 million self-employed people and sole traders in the UK, and 1.2 million businesses with at least one employee⁷⁰. That is 4.8 million in total. It is a fact, often noted, that if just one in 10 of these businesses took on an employee, or an additional employee, that would increase employment by 480,000.

69 Nesta, *Growth Dynamics: Exploring business growth and contraction in Europe and the US*, Albert Bravo Biosca, 2010, <http://www.nesta.org.uk/library/documents/GrowthDynamicsWebv3.pdf>

70 BIS: Business Population Estimates for the UK and Regions, 2012

- 5.11 My view is that the performance of our best companies is not where our problems lie. Our best are on a level with those in other countries. They can compete in world markets. It is essential, of course, for ministers to support the achievements of these companies in every way they can. In truth, though, they do not need much encouragement.
- 5.12 The big challenge we face, therefore, is in encouraging the growth ambitions and developing the capabilities of the remaining large mass of slower growing and lower performing businesses. These are the ones that ministers rarely get to see on their regional visits, focused as such visits are – invariably – on the high achievers. It is rare too, for ministers to get advice about these businesses, or to have a dialogue with them.
- 5.13 Indeed there are few formal structures within which a dialogue can take place. The UK’s business representative bodies only skim the surface of the business population because levels of membership and engagement are low, and the business voice is fragmented.

Table 5.1: Membership of generic business representative bodies

Total number of businesses in UK	4.8 million
Business representative bodies	Membership
British Chambers of Commerce	104,000
CBI	240,000
Federation of Small Businesses	200,000
Institute of Directors	43,000
Forum of Private Business	18,000
Engineering Employers Federation	6,000

Source: BCC, CBI, FSB, FPB, IoD, EEF

- 5.14 Yet these businesses are important. There are many more of them in the UK than there are high growth companies. Enhancing their capabilities would therefore make a huge difference to our economic prospects. The margins matter. Small improvements in productivity, if continuous and sustained over a period of time will make a significant difference to standards of living in the long term.
- 5.15 It is tempting for policy to focus on a few select, top-end sectors and on high growth companies. The fashion changes, but at the moment it is high tech and exports to the new markets that are paraded as the easy solutions. They are important, but ultimately they are not enough to ensure a broad-based competitive economy. We cannot ignore the performance and growth potential of the mass of businesses across all sectors including construction, logistics, retail, hospitality and health and social care, which have traditionally provided a high proportion of the employment opportunities in this country. As Table 5.2 shows, they will continue to provide a high proportion of our employment opportunities.

Table 5.2: Employment projections for 22 industry groups to 2020

	Absolute Levels (000s)			Changes (000s)
	2010	2015	2020	2010–2020
Agriculture	453	439	419	-34
Mining and quarrying	57	55	50	-8
Food drink and tobacco	401	402	404	2
Engineering	397	359	328	-69
Rest of manufacturing	1,719	1,687	1,616	-103
Electricity and gas	99	104	87	-13
Water and sewerage	158	172	190	33
Construction	2,092	2,189	2,329	237
Wholesale and retail trade	4,661	4,716	4,824	164
Transport and storage	1,424	1,460	1,519	95
Accommodation and food	1,892	1,975	2,049	156
Media	323	351	388	65
Information technology	773	774	795	22
Finance and insurance	1,092	1,106	1,159	67
Real estate	436	495	543	107
Professional services	2,280	2,475	2,668	389
Support services	2,353	2,579	2,671	318
Public admin and defence	1,544	1,346	1,428	-116
Education	2,703	2,623	2,663	-39
Health and social work	3,948	3,813	4,000	52
Arts and entertainment	856	948	1,055	198
Other services	796	789	825	29
All industries	30,458	30,855	32,008	1,550

Source: Working Futures 2010–2020 (p71), UKCES, August 2012

5.16 Suggesting that some businesses need to pull their socks up is controversial. A point eloquently made to me in the course of my review was that owners of established businesses would resent suggestions from Whitehall that they should show higher levels of growth aspiration. For many businesses, just maintaining existing turnover levels is a significant achievement – in current times, doubly so. They might feel that the messenger lacks credibility. What right does the Government have to call on established businesses to take on higher risks, to risk the shop, in order to chase growth?

5.17 The truth is that government exhortation will cut no ice. It is not going to move the boardrooms of Britain, and nor should it. The aspiration to improve and grow must come primarily from business and the business community itself. And once seeded, aspiration has to be allied with confidence – confidence in the business environment, and confidence that advice and support will be there to help turn aspiration into reality. It is here that government has a serious role to play, working in partnership with the private sector to ensure that businesses with aspirations have access to the advice, the networks, the finance and the support services that they need to grow.

The importance of business advice and support

5.18 There is a misleading myth, encouraged by recent television programmes, that entrepreneurs are born and not made. The entrepreneurial instincts need to be present, but it is nonsense to suggest that entrepreneurs and business owners do not need advice. They do. Only 50% seek advice, but the evidence shows that the companies which seek it are nearly twice as likely to grow as those that do not⁷¹.

5.19 A recent small business survey⁷² asked SME employers to rate their capabilities in a number of important business areas. The findings were instructive. Only 25% rated themselves as strong in accessing external sources of finance. Only 26% said they were strong in entering new markets. These are areas of business competence that are central to growth capacity, and areas where businesses could clearly benefit from advice.

5.20 The key to raising the performance of business is in part, therefore, to raise the demand for advice. There is no shortage of supply. It comes from many quarters – from banks, accountants, a myriad of consultants, government and others. Much of it is good and fit for purpose.

5.21 There are many reasons for the shortage of demand. Some businesses are not able to diagnose their business support needs accurately. Some will be unaware of the information and advice that is available. Some will be uncertain about its suitability and the benefits it can bring. There can be a lack of trust in the providers. Consultants can be tempted to provide easy solutions, irrespective of the nature of the problem presented, leaving a legacy of mistrust.

5.22 If we are to drive up demand and build business capability, we must try to overcome these market failings. We need a radical improvement in how businesses are engaged and supported at a local and sectoral level. We need to ensure that all businesses have easy access to business support and advice that they trust. In short, we need a coordinated business support infrastructure, led by the private sector, that is accessible to all and which will stand the test of time.

⁷¹ BIS, *Small Business Survey*, 2010

⁷² *ibid*

5.23 Many attempts have been made to improve and rationalise the business support environment. We have been through the experience of Local Employment Networks, the Training and Enterprise Councils (TECs), and Chambers of Commerce Training and Enterprise (CCTE). Most recently the Business Link face to face network was disbanded as part of the process of winding up the Regional Development Agencies. Despite these efforts, none of these initiatives survive today.

The role of chambers of commerce⁷³

5.24 Our competitor economies have been more successful. They have achieved a far more coherent and consistent approach to the organisation of private sector-led business advice and support. Often it is a support system centred on powerful and well resourced chambers of commerce with high levels of business membership.

British Chambers of Commerce (BCC) and the accredited chamber network

BCC is a national umbrella body owned by, and acting for, 51 local chambers of commerce across the UK (the BCC-accredited chamber network).

BCC status: No special legal status, other than the rights conferred to it under the Company and Business Names (Chambers of Commerce, etc) Act 1999, which gives it a power to regulate the use of the chamber name in the UK. This power does not allow the BCC to regulate those using the chamber name before 1999.

Membership: Membership of the BCC by chambers of commerce in the UK is voluntary. Currently, there are 51 chambers in the BCC-accredited chamber network.

Membership of chambers: Membership of chambers of commerce by businesses is voluntary. The BCC-accredited chamber network collectively has 104,000 business members. Between them, the members employ 5 million people.

Membership profile: Inclined towards businesses that are employers, exporters, manufacturers and business services providers.

Non-affiliated chambers: In addition, there are up to 600 local chambers (e.g. town chambers) that are not affiliated to the BCC.

Overseas presence: There are 63 overseas chambers. These have been established independently, operate independently of each other, and are incorporated either in their host countries or in the UK. They are not managed or regulated by the BCC.

⁷³ A supporting paper on chambers of commerce has been prepared to accompany this report. <http://www.bis.gov.uk/assets/biscore/corporate/docs/n/12-1214-no-stone-untuned-chambers-of-commerce-international-comparisons>

- 5.25** Of course, we have our own chambers of commerce, but they operate on nothing like the scale of many European chambers, and without any statutory backing or special recognition from government. Total membership is 104,000 out of a total of 4.8 million businesses. In contrast, the Paris Chamber of Commerce alone has 400,000 members, and those in Munich and Milan each have memberships considerably in excess of 300,000.
- 5.26** Germany is often singled out as having the most effective and integrated business support infrastructure. In that country, membership of a chamber of commerce is compulsory for the vast majority of businesses, and a typical chamber will have a business membership of more than 30,000. Contrast that with the position in this country where the largest single chamber – the Greater Manchester Chamber of Commerce – has about 5,000 members.

German Chambers of Commerce

Legal status: Main mission is defined in statute with membership compulsory for most businesses.

Public duties: To promote the economic interests of local businesses; provide information, advice and support to businesses; issue trade documentation; and manage the business register.

Number and membership levels: There are 82 local chambers (IHKs) with total membership of 3.6 million businesses. They are supported by 7,000 dedicated experts specialising in areas such as commercial law, trade, training and arbitration. 400,000 individuals work on a voluntary basis.

Overseas presence: There are 117 overseas chambers (AHKs), responsible for promoting trade and winning foreign investment. The German chamber in India, for example, has a network of 6,000 businesses. (The UK in contrast has no chamber in India).

Services provided: These include the provision of in-company vocational training programmes, disseminating national level information, issuing certificates of origin for international trade, provision of expert advice and inputting into municipal budgets, tax regimes, planning and infrastructure decisions.

Interface with central government: The local chambers are supported by a national level organisation, known as the DIHK, which interfaces with the German national government.

An integrated whole: The local, national and international chambers present themselves to business as part of a single family.

- 5.27** Germany is not alone. France, the Netherlands and Japan all have well co-ordinated chambers underpinned by law. In Japan there are more than 500 chambers of commerce, and 79 based overseas. About a third of all Japanese businesses are members of chambers, despite Japan having a voluntary membership model.
- 5.28** What is striking when looking at other chamber models is the degree of consistency and continuity these networks have been able to provide. For decades, businesses have known that there is always an organisation they can turn to for advice both at home and overseas. The chambers in these countries act as a spine on which capability and experience can be built over time. UK businesses have had no such continuity. The UK approach to business support is constantly changing. Organisations, programmes and services come and go, leaving little long term legacy.
- 5.29** Not every country structures its business support around chambers. The US, for example, has a chambers network, but also the Small Business Administration (SBA), an independent agency of the federal government, which operates in every state, and aims to encourage and develop small business growth.

US Small Business Administration (SBA)

The SBA was established in 1953 through the Small Business Act to encourage and develop small business growth.

It operates throughout the US through an extensive network of field offices and partnerships with public and private organisations.

It provides a number of services and programmes for small businesses, including: guarantees to support loans; advice on international trade; face to face and online advice on starting, managing and developing a business through small business development centres; and advice on federal contract procurement opportunities.

It draws heavily on active and retired entrepreneurs through the SCORE network to deliver advice and ongoing support to existing and aspiring entrepreneurs. SCORE is a non-profit association comprising some 11,500 volunteer business counsellors.

- 5.30** Hong Kong has a long established Hong Kong Productivity Council – a public and private sector partnership – which aims to provide integrated support to SMEs.

Hong Kong Productivity Council

- The Hong Kong Productivity Council (HKPC) is a multi-disciplinary organization established by statute in 1967. Its mission is to promote productivity through the provision of integrated support across the value chain of Hong Kong firms in order to achieve a more effective utilization of resources, to enhance the value-added content of products and services, and to increase international competitiveness.
- HKPC has a governing council which represents managerial, labour, academic and professional interests, as well as related government departments. The operation of HKPC is supported by fee income from its services and government subventions.
- HKPC's headquarters in Kowloon Tong features various advanced manufacturing and testing facilities as well as exhibition and training venues. HKPC also operates three wholly owned subsidiaries in mainland China to serve Hong Kong manufacturers in the Pearl River Delta.
- HKPC has more than 200 professional consultants who, together with its subsidiaries provide a multitude of services in technology transfer, consultancy, training and other support services in the areas of manufacturing technology, information technology, environmental technology and management systems.
- HKPC has partnerships with a range of private sector organisations, including HSBC Hong Kong which runs a Wise Business programme to support SMEs. The bank provides free one-on-one consultancy services and large scale customer seminars.

Vision for a new business support infrastructure

- 5.31** Each country provides support in its own way, but what is striking is how unusual the UK is amongst advanced industrial countries in not having a strong and stable business support infrastructure. We should address this deficiency.
- 5.32** My solution is to build a business support infrastructure in this country, based around chambers of commerce. Some will ask, why the chambers? My answer is that they have unique strengths and characteristics on which we can build.
- First, they are remarkably constant. Chambers of commerce have been in existence in the English-speaking world since the 1760s⁷⁴. The concept has proved resilient enough to survive countless changes of circumstance and government initiatives.

74 Robert J Bennett, *Local Business Voice*, p15, Oxford, 2012

- Second, chambers have a unique international status. They have foreign counterparts and are supported by an International Chambers of Commerce that helps broker international trade agreements and arbitrates disputes. Importantly, having the same established, recognised brand in a foreign market and in the UK can facilitate the journey for a business wanting to expand and grow its export operations.
- Third, they are based in local business communities and are locally led. The services they provide are aimed at all businesses irrespective of size or sector. They are therefore different to the sector-based organisations and the national business lobby groups. Chambers are recognised democratic institutions often contiguous with the geography of local authorities and Local Enterprise Partnerships (LEPs) – and could become more so. They are uniquely placed to partner LEPs in taking forward the practical business support elements of the local economic plans described in Chapter 2.
- Fourth, chambers are independent, business-led entities. All the evidence suggests that businesses prefer to engage with their peers not with government. Chambers are well-placed to encourage the networking between businesses that is likely to increase their aspirations and capabilities.
- Fifth, they have an existing infrastructure and service delivery capabilities which could be built on. UKTI, for example, already contracts directly with chambers in seven out of nine regions to deliver the government's export advice services. Another example is the contract that the Skills Funding Agency has in place with the North East Chamber of Commerce to deliver apprenticeships.

North East Chamber of Commerce (NECC) – Apprenticeship service

The NECC has a £3 million contract with the Skills Funding Agency to deliver apprenticeships. The chamber has two teams: one persuading businesses to take on apprentices; the other persuading young people to become apprentices.

NECC puts all apprenticeship candidates through assessments, with employment readiness training provided where needed. Candidates also receive help from the chamber with CV preparation.

Businesses wanting to engage an apprentice are provided with 6–12 CVs, and help with sifting and interviewing. The NECC team also ensures that the business understands the relevant employment law relating to apprenticeships.

- Sixth, chambers are built on a volunteering model. Many local business people volunteer their time freely to chambers to act as mentors for example. This is an important dimension that sets chambers apart from many other bodies.

- Finally, chambers have an established youth chamber network to help build young people's understanding of business, and to give them hands on experience of enterprise and the business world.

5.33 The international dimension to the chambers' work is critical. If we are to accelerate the internationalisation of our economy and achieve the target that the Government has set of doubling exports to £1 trillion by 2020, we need to galvanise much more of industrial and commercial Britain. Chambers can be at the heart of this push both domestically but also using their overseas capacity. I strongly support the efforts of the Trade Minister in the work he is doing to strengthen the chamber movement in pursuit of this target. In my view, the Government will find it very difficult to get near its ambitious export targets without infrastructure support of this kind.

5.34 Of course, the chambers as they currently operate have their critics. Like other business representative bodies, they suffer from low membership levels in the business community. There are many examples of good practice and service provision, but also suggestions that there is inconsistency. Some point to an image and diversity issue – that membership of a chamber, whether rightly or wrongly, is perceived as being for a certain type of business or not a place for dynamic, high growth companies to go to for support.

5.35 Some of the criticisms of the chambers may be justified, some not. I am not though interested in assessing chambers as they are, but rather in what they can become.

5.36 I see the chambers as being at the heart of a local, business-led support infrastructure: where they have far higher levels of membership and real influence; and where they are helping to galvanise the performance of a far broader range of businesses. I envisage them having a central role:

- working as the LEPs' delivery partners, taking responsibility for co-ordinating and organising the delivery of the business support services set out in each LEP's local economic plan
- providing a one stop shop for businesses so that they have easy access to business services, including practical advice and support on exporting and training and access to business networks and mentors
- acting as a focus for business engagement with the wider community, particularly engagement with schools and colleges
- using their increased legitimacy as broad-based business bodies to go toe to toe with decision-makers. They will have the clout to put wealth creation at the centre of local agendas, influencing decisions about infrastructure, planning and other aspects of the local business environment

- > providing central government with a streamlined route for engaging with local business communities
- > providing advice on routes to international markets for small and mid size companies.

5.37 Chambers could also be involved in advising on, brokering and organising apprenticeships and articulating business skills and training needs. In addition, they could build links with local business schools to improve leadership and management capabilities. I return to these issues later in the chapter and again in Chapter 6.

Table 5.3: Illustrative menu of services that could be offered by local chambers operating in partnership with LEPs

Business support	Wider engagement	Influencing the local business environment
Export advice (including trade documentation)	Building links with overseas chambers in key growth markets	Hot line to the LEP
Advice on finance and on apprenticeships	Developing business and education partnerships	Advising LEP on business support products needed to meet local needs
Access to:	Providing careers advice in schools	Defining and aggregating local skills and training needs
> local mentors, business clubs and other networks	Facilitating work experience, internships, and FE/HE placements	Making representations on planning decisions
> the local banking and investment community	Accessing FE college and HE networks	Articulating local infrastructure needs
> international chamber networks and overseas local market contacts	Identifying and training volunteer business mentors	Dialogue with local regulators
> information on central and local government procurement contracts		
> local and central government business support products		
> information on EU-funded programmes where applicable		
> Support for building leadership and management skills		

5.38 Some may ask about the position of other business representative bodies and whether they will be adversely affected by putting chambers at the heart of the LEPs' local plans for business support. Looking abroad, I am confident that this will not be the case. I see no reason why chambers and other business organisations cannot co-exist, and indeed be mutually reinforcing. That is the case in Germany, France and the Netherlands where chambers are hub organisations linking to wider sources of advice and support where necessary. If our chambers can succeed at the local level in raising business aspirations and stimulating demand for advice then, with appropriate coordination, a range of different business organisations will be able to benefit from the additional demand that ensues. I would expect chambers and other business bodies to collaborate closely and creatively at local level – far more than they do at the moment – to ensure that business support provision as a whole is greater than the sum of its parts.

International examples of collaboration between business bodies

Business bodies in other countries have taken steps to co-locate or share back office services to improve collaboration and improve cost-efficiency.

- In Germany, the head offices of the chambers, the employer federations and the German equivalent of the Trade Association Forum are all co-located in the same building.
- In the Netherlands, the Dutch equivalents of the CBI and the FSB have merged their back offices.

5.39 I realise my proposals are controversial. But if we are going to reach out to the range of companies who belong to none of the existing organisations, some equivalent to the methods used successfully overseas seems essential. The status quo does not work, and no one I know believes it does. Newly invigorated, effectively led and properly resourced chambers, drawing on the disparate strengths of the other local business bodies would give a new private sector-led focus to improving our national performance.

How do we get there?

5.40 There is no reason why all this should be beyond us, why we should not be able to emulate best practice amongst our competitors in Europe and elsewhere. We do not need to copy every feature of the overseas models. We should be in the business of picking out the best elements, and adopting them in a way which reflects our culture and heritage. Where there is a will there will be a way.

5.41 If the chambers are to have an enhanced status, and able to act as the co-ordinating hub for business services and engagement they could benefit from being given a stronger formal status through legislation. Enshrining chambers' existence and basic functions in legislation would provide greater assurance of stability and continuity, and provide the

confidence needed for chambers and their members to invest time and energy in developing the network.

Chambers of commerce – illustrative list of legal functions and duties

The functions of chambers of commerce could be to:

- > promote the economic interests of local businesses
- > facilitate the provision of information, advice and support to local businesses
- > provide a channel for the communication of national and local government information to business and visa versa.

Chambers could also be required to ensure that:

- > every business has the opportunity to join a chamber
- > their constitutions are democratic
- > the network as a whole is organised in a way that is rational and efficient, aligned wherever possible with functional economic market areas.

The law could guarantee the independence of the chambers from government.

5.42 Chambers themselves will need to consider how they are organised locally to ensure they have sufficient scale and an effective interface with their local LEP and the business community it represents.

5.43 Chambers are quite rightly suspicious that government will encourage them to build the staff and infrastructure to implement these ideas and then lose interest, change its mind, or be replaced by a different government leaving them to pick up the costs of scaling back down. The chambers have been bruised before. Recognition in statute will help. In addition, there will be ways of providing reassurances of continuity in the economic plans that LEPs will draw up for their areas which will be for five year periods. Where necessary, arrangements should be made to compensate chambers when plans change unexpectedly. It is essential that the chambers' legitimate fears on this score are addressed.

Recommendation 63: The chambers of commerce could benefit from an enhanced legal status to support their role as coordinating hubs for business support and engagement at local level. The Government should consider legislating to give chambers basic statutory functions, whilst guaranteeing their continuing independence from government. It should provide for compensation if government opts out of these arrangements.

5.44 There is a choice to be made between making chambers membership compulsory for businesses, or keeping it voluntary. In France and Germany, the law makes membership for most businesses compulsory. In Finland, Japan and Sweden, chambers have certain statutory functions and a legal status, but membership is voluntary and is correspondingly lower. The impact this can have on membership levels is illustrated in table 5.4.

Table 5.4: Effect of legal status on membership levels for chambers

Country	Voluntary membership models			Compulsory membership models		
	UK	Finland	Japan	Germany	France	Netherlands
Membership	104,000	18,000	1,300,000	3,600,000	2,200,000	2,300,000

Option 1: Compulsory membership

5.45 Compulsory membership would provide the reach and membership levels that have eluded business membership organisations hitherto. It would provide chambers with an assured status and stability, a national network, and a larger pool of resources to attract and retain management talent. Subscription income would significantly boost the ability of chambers to provide business services entirely independently of government. To illustrate the point, the Munich Chamber of Commerce had an annual income of more than £65 million in 2011. The equivalent figure for the Birmingham chamber was £10.6 million.

5.46 Compulsion rather than voluntarism would be unpopular. Although aimed at improving private sector capability, compulsion would represent a new regulatory requirement for business and would involve payment of membership fees. Important practicalities, not relevant in a voluntary system, would need to be addressed. What, for example, would be the trigger point for membership, and how would this be enforced? PAYE or VAT registration would be possible triggers and would automatically exempt the very smallest businesses from membership. A further possibility would be to link membership to the payment of local business rates. This has attractions in that enforcement could be aligned with existing arrangements for collecting business rates. These and other options would need to be explored further.

Option 2: Voluntary membership

5.47 The second option would be to retain a voluntary membership system, possibly combined with legislation (either immediately or in due course) to give chambers basic statutory functions.

5.48 Rather than push companies into becoming members of chambers, this option would seek to pull them in and make it worth their while to join. The challenge for chambers would be to exploit their enhanced status at the heart of the LEPs' local economic plans

and build a compelling service offering such that every business would see the advantage of chamber membership.

- 5.49** The effectiveness of this option would depend to a degree on the willingness of the private sector to subscribe to the vision of a strengthened chambers network. However, as I have recommended in Chapter 2, I envisage significant resources being made available to the LEPs to promote economic development in line with local economic plans. There will therefore be real opportunities for chambers to develop a compelling local offer for businesses in partnership with their local LEP.

Recommendation 64: Government and the private sector should collaborate to create a strong and stable, locally-based, private sector business support infrastructure. This should be centred on an enhanced role for chambers of commerce. At the minimum, government should pursue option 2 and take all appropriate steps to secure its implementation.

Publication of business rates data

- 5.50** Whichever system – compulsory or voluntary – is ultimately preferred, chambers will need enhanced tools to enable them to identify businesses in their area, and pull them into the local business support infrastructure. Many businesses are well established, and have a strong local profile. Others will be far less visible, and will not necessarily be known to the chambers or, indeed, to the other business representative bodies. The solution lies locally, because each local authority holds a comprehensive list of all businesses paying non-domestic rates.

Recommendation 65: Local authorities should publish the list of all businesses paying non-domestic rates so that chambers and other business representative bodies can identify businesses in their area more reliably, and seek to draw them into the local business support infrastructure. There should be exceptions for businesses where the identification of business premises could give rise to security concerns.

Trade associations

- 5.51** Specialist trade associations are an important part of the business support landscape, and an important way in which business can help itself. They are sector-based, and play a distinct role to that of chambers and other business representative bodies such as the FSB and the CBI.
- 5.52** Trade Associations have two main purposes. First, they aim to provide a co-ordinated voice for sectors when talking to government. They can help ensure that government decisions in areas such as regulation, standards and skills take heed of the sectoral impacts. Second, they have an important role in improving sectoral performance through activities such as training, skills development, benchmarking, mentoring and supply chain

development. All too often, however, the role trade associations can play in developing the capabilities of their member companies is neglected in favour of lobbying. In the nature of things, that can encourage a dialogue that is centred on the problems of the slowest ships in the convoy.

Role of the Trade Association Forum

- 5.53** I have set out my ideas for building stronger relationships between trade associations and government in Chapter 3. That chapter also sets out steps that government itself can take to encourage the rationalisation and improvement of trade associations through the nomination of lead associations. In this section of the report, I focus on the steps trade associations themselves can take to improve their capabilities.
- 5.54** Trade associations can do much to raise their performance by sharing best practice and learning from each other. That was the rationale for the establishment of the Trade Association Forum (TAF) in 1997 with initial financial backing from the then DTI and the CBI. The Forum is an umbrella organisation with about 300 members, a fraction of the 3,000 trade associations in the UK.
- 5.55** It has done much useful work. For example, it developed a best practice guide for a model trade association which has been used by many associations to benchmark themselves against others and as a blueprint for restructuring and reform⁷⁵.
- 5.56** The TAF is currently updating its Code of Practice to bring it into line with the statutory register of lobbyists. This new Code will set minimum recommended standards for trade associations. These standards could be given additional teeth by making them requirements for membership of the TAF. Each application for membership could be reviewed by the TAF in conjunction with an independent panel. The TAF would therefore be taking on a quasi accreditation function.
- 5.57** The development of the Code should be industry-led, but with input from government. Standards should not unreasonably act as a barrier to new entrants, and should be phased in to allow TAF members to make the transition. The Code should include a requirement for trade associations to demonstrate a commitment to improving the performance of their sector, as well as covering their lobbying functions.

Recommendation 66: An updated Code of Practice for Trade Associations should be developed. It should be given teeth by making compliance with the Code a condition for membership of the Trade Association Forum.

⁷⁵ <http://www.taforum.org/a->

- 5.58** The TAF is currently working with external consultants⁷⁶ on the development of a competency framework for individuals working in trade associations. This will help drive up professionalism, create credible career paths and make it easier to attract high calibre individuals. It is a welcome development.

Recommendation 67: The Trade Association Forum should press ahead with the development of a competency framework for individuals to drive up professionalism within trade associations.

- 5.59** Trade associations do not currently have to register anywhere. The TAF compiles a directory of its members, but it is not comprehensive, nor is it easy to navigate. An enhanced directory, navigable through keyword searches, would facilitate better partnership working across the trade association community. Crucially, it would make it easier for businesses to identify trade associations of interest to them. It could form the first reference point for government officials seeking to understand the structure of trade associations in a particular sector. It could also help with the identification of the lead trade associations and umbrella groups recommended in Chapter 3 where recommendations are made for improving links between government and industry.

- 5.60** All trade associations which have met the minimum TAF membership standards should be automatically included in the directory, and they should be differentiated from non-accredited associations.

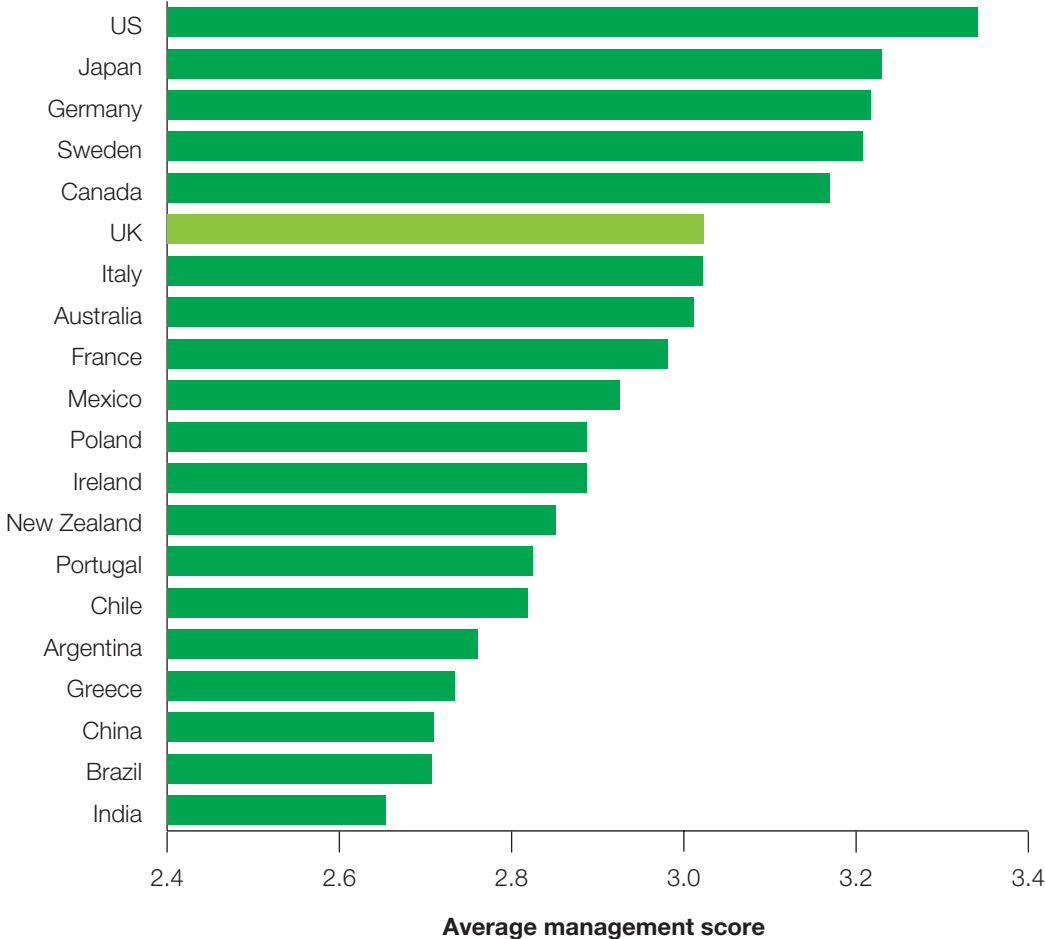
Recommendation 68: The Trade Association Forum should develop an enhanced directory of associations which is easily navigated through keyword searches.

Leadership and management

- 5.61** Whatever support businesses receive, businesses need the capabilities to use that advice to deliver sustained growth and improved profitability. Concerns about weaknesses in the management and leadership capabilities of UK businesses have been with us for some time. They were a feature of the Competitiveness Reviews carried out by the Government in the 1990s, and these concerns continue to this day. We have not cracked the problem.
- 5.62** Our overall performance in leadership and management is mid-table by international standards, and our score is dragged down by a persistent tail of underperforming businesses – a tail that appears to be largely absent in the US.

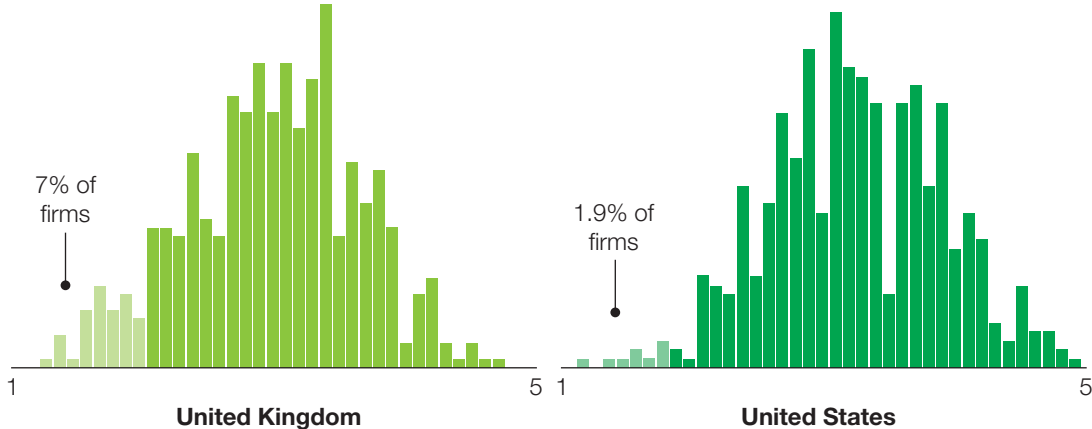
⁷⁶ MemberWise and The Professionalism Group

Chart 5.3: International comparison of leadership and management capabilities



Source: BIS, *Constraints on Developing UK Management Practices*, 2011. Comparison based on management interviews between 2006 and 2010

Chart 5.4: Extended tail of UK companies with weak management practices



Source: BIS (see Chart 5.3)

- 5.63** Leadership and management matters hugely to business performance, regardless of size. It is a key factor in ensuring that businesses have the right strategies in place to drive growth. It is also an important factor in fostering innovation and unlocking the full potential of employees. CBI employers cite it as the most significant factor contributing to competitiveness. Indeed there is a body of academic research which suggests that weaknesses in this area are one of the causes of our productivity gap with countries like the US, Germany and Japan⁷⁷.
- 5.64** There is also a school of management research which suggests that, in order to grow, businesses have to traverse a series of tipping points, with success very much dependent on a business's internal capabilities. They relate to taking on staff, strategy formulation and execution, formalising systems, entering new markets, obtaining external sources of finance, and driving operational improvement. Businesses with strong leadership and management are far better equipped to overcome these obstacles. They also appear to be more likely to seek out and exploit advice from external sources, and have a higher capacity to absorb that advice when they receive it.
- 5.65** At one level, there appears to be no shortage of growth ambition amongst our SME population. 74% of SME employers have aspirations to grow over the next two to three years⁷⁸. However, the reality is that only about a third of businesses actually grow in terms of turnover, and about a fifth in terms of employment. Stronger leadership and management skills could allow more businesses to realise their ambitions.
- 5.66** Steps are being taken to address these weaknesses. The development of leadership and management skills are central to the Government's Growth Accelerator programme aimed at smaller businesses with high growth potential⁷⁹. The Government's growth review of mid-size businesses led to the establishment of a Business Schools Task Force. This is considering how business schools can develop the management skills of mid-size businesses. UKTI has adapted its Gateway to Global Growth programme to build in a management component for mid-size businesses. In addition, a number of LEPs have taken the initiative to develop business networks between mid-size businesses in their local area. Finally, resource is being made available for leadership and management training via the Employer Ownership pilot and the Growth and Innovation Fund which allow business clusters to develop solutions to meet their skills needs.
- 5.67** These are steps in the right direction, but there is much more that could be achieved by tackling leadership and management capabilities more widely at the local level. A good example is Northumbrian Water which organised a leadership training day for businesses

⁷⁷ Bloom, N, Van Reenen, J, 'Measuring and Explaining Management Practices Across Firms and Countries', Quarterly Journal of Economics, 2007; Homkes, R (2011). Bloom N, Lemos R, Qi M, Sadun R, Van Reenen J, *Why Management Practices Matter for Productivity and Competitive, and what It Means for Government Policy*, Centre for Economic Performance, 2011

⁷⁸ BIS, *Small Business Survey*, 2010

⁷⁹ Participants on the programme have access to grant funding of up to £2,000 per individual for use on management and leadership training which has to be fully matched by the beneficiary

in its local supply chain. The supply chain responded in numbers to its main customer. These locally driven initiatives can be highly beneficial. There is a role for chambers as a catalyst for these sorts of events – persuading local businesses to contribute and participate. Where there is no coherent supply chain led by a large company, these networks are best developed at the local level.

- 5.68** Where LEPs identify leadership and management capability as an issue for businesses in their areas, I would expect their economic plans to reflect this. The work could be led by the chambers of commerce, making full use of local business networks and the strengths of business schools and other training providers in the area.

Recommendation 69: In developing their economic plans, LEPs and chambers should consider ways in which leadership and management capabilities in local businesses can be raised making full use of local networks, local training providers and businesses themselves. Plans could, for example, incorporate commitments from large corporates and leading mid-size businesses to help raise leadership and management capacities in their supply chains.

- 5.69** Government has an important role in determining the schools curriculum. Along with Higher Education institutions, it also determines the content of a wide range of qualifications, from school level exams, through to apprenticeships and other vocational qualifications and higher level degrees. Given the consensus around the importance of leadership and management skills to economic performance, training in these skills should be built into the education and training system wherever it makes sense to do so.

Recommendation 70: The development of leadership and management skills should be integrated, where appropriate, into the education and skills system at every level, from schools through to higher education and vocational skills training. We need to see individuals having opportunities to develop their leadership and management capabilities earlier on in their working lives, alongside the development of technical or academic competencies.

The importance of supply chains in raising performance

- 5.70** Who does a business owner really listen to? Who ultimately has most influence? The answer comes back that it is the customer – and the biggest customers, in particular – who matter most and carry the greatest influence.
- 5.71** The large companies that sit at the head of supply chains can have a huge influence on the quality, performance and prospects of their suppliers and the companies beneath them. They can also have a significant impact in providing leadership for their sectors in times of transition. They provide a rainforest canopy supporting a whole ecosystem of

businesses – large, medium and small. We should not look at SMEs, or mid-size businesses, or large businesses in isolation. They are closely inter-connected.

- 5.72** The Rolls-Royce and Jaguar Land Rover supply chains illustrate how important the prime customer is in supporting a complex ecosystem of business life.

Rolls-Royce – UK supply chain

Prime

- Rolls-Royce has 3,000 UK-based suppliers
- Its annual spend with UK suppliers is c. £2.5 billion⁸⁰

Tier one

- Rolls-Royce's top UK-based aerospace supplier is Pattonair
- In total, Pattonair has 235 UK-based suppliers

Tier 2

- Pattonair's three largest suppliers have, between them, more than 270 UK-based suppliers

Tier 3

- The supply chain continues down several further tiers

Jaguar Land Rover (JLR) – UK supply chain

- JLR has nearly 2,000 UK-based suppliers. Of these, 235 are production suppliers (with some or all sites in the UK); 1,732 are non-production based suppliers.
- JLR's total annual spend on UK-based suppliers is c. £5 billion⁸¹.
- IAC (International Automotive Components) is one of JLR's largest tier one suppliers. It alone has more than 100 UK-based suppliers.

- 5.73** Rolls-Royce and JLR are examples of companies with an excellent record for nurturing and developing the UK businesses in their supply chains. JLR, for example, has opened its engineering Masters programme to companies in its supply chain. There are other exemplar companies such as Toyota and 3M.

80 Rolls-Royce 2011 data – all UK purchases

81 Most recent 2012/13 estimates from Jaguar Land Rover

5.74 More of our large companies could commit to expanding the number of UK-based companies in their supply chains, and then working with them to develop their quality. More of them could play a role in mentoring supply chains in key business skills such as leadership and management or increasing innovation from suppliers. They could help trade associations develop sector-wide skills programmes. Government too, has a role to play with inward investors, in being more insistent that they make use of and develop domestic supply chains.

Recommendation 71: As part of their growth commitments, departments should set out plans for sector-based supply chain programmes, learning from the experiences of the Advanced Manufacturing Supply Chain Initiative.

5.75 There are interesting ideas in Tim Breedon's Review, Boosting Finance Options for Business⁸², for encouraging prompt payment and supply chain financing techniques to reduce reliance on bank loan facilities. He also sees scope for larger companies to make financial investments in their smaller suppliers to facilitate their expansion. I support these ideas.

Access to finance

5.76 Businesses' ability to access the capital they require to invest and grow is crucial to the future health of our economy.

5.77 There is clearly a current cyclical problem. All commentators agree that the flow of loans has been in decline since the credit crunch struck, a trend starkly illustrated in Table 5.5 from the Bank of England's Trends in Lending report which shows a sharp net reduction in lending to business. Further evidence comes from the SME Finance Monitor⁸³. Data for the second quarter of 2012 revealed that only 43% of SMEs were using external finance compared to 51% at the equivalent point a year ago.

82 Breedon Review, 2012,

<http://www.bis.gov.uk/assets/biscore/enterprise/docs/b/12-668-boosting-finance-options-for-business.pdf>

83 *SME Finance Monitor Q2 2012*, <http://www.sme-finance-monitor.co.uk/>

Table 5.5: Lending to UK businesses (PNFCs) by UK monetary financial institutions

	Averages							2012		
	2007	2008	2009	2010	2011 Q4	2011 Q1	2012	Mar	Apr	May
Net monthly flow (£ billions)	7.4	3.8	-3.9	-2.2	-0.8	0.1	-3.2	-2.0	0.4	-1.7
Three-month annualised growth rate (per cent)	20.8	10.7	-7.7	-5.2	-2.0	0.2	-6.3	-8.2	-4.9	-2.9
Twelve-month growth rate (per cent)	16.8	17.9	-1.8	-7.1	-3.3	-2.1	-2.9	-3.2	-3.5	-3.1

Source: Bank of England Trends in Lending, July 2012.

- 5.78** There does not appear to be a definitive answer as to whether this decline is due to a lack of supply from banks or limited demand from businesses lacking confidence. I must confess that I started with the prejudice that accessing bank finance is largely a demand rather than a supply problem. I felt that businesses with a worthwhile proposition, sensibly set out, will generally secure the bank finance they need. I am less confident now.
- 5.79** The Breedon Review⁸⁴ which was set up to explore the range of alternative options to bank finance, particularly for SMEs, found that supply and demand is generally in equilibrium at the moment because of a lack of confidence and suppressed demand. However, it had grave concerns about whether supply will be able to meet future demands for finance as the economy recovers. The review estimated that the finance gap could be between £84 billion and £191 billion over the next five years. The banks' ability to respond will be adversely affected by the cumulative impact of continued deleveraging, the declining value of collateral, and tougher capital and liquidity requirements arising from Basel III.
- 5.80** The Government has rightly devoted significant energy to improving the price and availability of credit to businesses to tackle both cyclical and longer term structural issues. The Enterprise Finance Guarantee, for example, does an important job of facilitating credit for those viable businesses that can service the debt on loans but do not have sufficient collateral, or track record, to secure the finance in the first place. The new Funding for Lending scheme from the Bank of England and HMT is a welcome attempt to support demand for finance by reducing the cost of credit whilst injecting more liquidity into the market. It is estimated that this could have the effect of releasing £80 billion of cheaper credit to households and businesses. This, however, as all acknowledge, is a temporary measure.

84 Breedon Review, 2012, p12

- 5.81** A more permanent, and therefore more satisfactory prospect, appears to be the new Business Bank whose formation was announced recently by the Business Secretary. We await greater detail on what it will do as the devil is certainly in the detail. But I am encouraged by the emphasis it will place on supporting competition amongst business finance providers and on the provision of long term, patient capital.
- 5.82** Public equity and venture capital are important for business growth. We must ensure that these markets are vibrant. I therefore welcome the Science Minister's recent announcement of a new route to the UK IPO market for high-growth companies which should be of particular benefit to British and other European mid-size companies. I welcome too the Government's Enterprise Capital Fund and UK Innovation Fund which are examples of successful partnerships between the public and private sectors, leveraging additional private sector co-investment to create funds of reasonable scale focused on companies operating in the equity gap. The Business Bank should continue to support the Government's activity in this area.
- 5.83** Whilst venture capital is important, many business owners are reluctant to dilute their equity and cede control to outsiders. I know from my own experience that this is the understandable mentality of many entrepreneurs and business owners. It is therefore desirable that our growing businesses also have opportunities to access long term loan capital.
- 5.84** Unfortunately, it is anticipated that one of the effects of the new Basel III rules will be to shorten loan tenors and reduce the willingness of banks to provide long term financing. Banks will be required to hold greater capital against assets, reducing returns and increasing pressure on their margins. This may exacerbate behaviour already being observed in the market which is seeing some major banks walking away from long standing relationships where there are now insufficient returns. The banks are likely to gravitate towards providing shorter duration loans (which have less costly capital requirements) in favoured sectors where returns are more predictable. Their focus is likely to be on quality credit borrowers who fit their strategic objectives and who are able to offer the prospect of ancillary income. All this points to structural weaknesses in the provision of longer-dated debt products for growing businesses who do not have these characteristics.
- 5.85** In contrast, growing businesses in countries like the US and Germany are able to access long term loan products either directly or indirectly through support provided by the US's Small Business Administration (SBA) or German's KfW⁸⁵. The SBA, for example, currently has a portfolio of more than 200,000 business loans worth more than \$45 billion. We need to address this deficiency in the UK.

85 The KfW is the German government's business development bank. It does not generally lend directly to enterprises, but provides commercial banks with liquidity at low rates and long maturities

- 5.86** I am attracted to the idea of recreating some of the elements of the Industrial and Commercial Finance Corporation (ICFC). It was set up in 1945 by the Bank of England with funding from the major commercial lenders to provide capital to small and medium-sized enterprises. It was driven by the government of the day which recognised that smaller businesses faced a funding gap due to banks being unwilling to provide long term capital and the companies being too small to raise capital from the market.
- 5.87** The ICFC provided long term debt and, latterly, equity to UK businesses. It operated through a regional branch network in places such as Birmingham, Manchester, Leeds and Leicester, and with staff who acquired expertise in particular firms and sectors. The regionalisation of the ICFC was partly the result of a desire to recreate the 19th century conditions of local investment that had been lost in the centralisation of investment through the London Stock Exchange. Good relationships were established with businesses at a local level with business loan applications being assessed on their merits, rather than by applying aggregated sector risk models. It invested for the long term, free of short term pressures.
- 5.88** Over time, the ICFC's focus shifted away from its original rationale towards larger and more cost-efficient deals, and was eventually floated as 3i. The original purpose and mode of operation, however, seem relevant to the position we face today.
- 5.89** An idea put to me in the course of the review was to look at the possibility of expanding the remit of the bank-owned Business Growth Fund (BGF) so that it could take on more of the characteristics of the ICFC. The BGF is owned by the main UK-based banks. Its current focus is entirely on equity investment, but it could be transformed into a provider of both long term debt and equity in a partnership with government. It would not be a mass market provider of loans, but could target firms seeking long term debt to match long term investments.

Current operation of the Business Growth Fund (BGF)

- The BGF is a fund owned jointly by five shareholder banks – HSBC, Lloyds BG, RBS, Barclays and Standard Chartered. It was set up in May 2011 with a £2.5 billion balance sheet.
- The fund currently provides equity-only investment of between £2–10 million for firms with up to £100 million turnover. It aims to take a minority share and hold its investments for 5–7 years.
- The BGF is aiming for 30–40 equity investments per year. It has a direct to market distribution channel, based in six regional offices covering the whole of the UK and is developing local networks with banks, businesses and advisers.

- 5.90** There seems to be a point in the growth of a typical UK business where sale becomes inevitable. This seems to be part of the business culture. Business owners must be able to realise the fruits of their entrepreneurialism and hard work. There is nothing wrong with that, but we do need to tackle the sense of inevitability. Particularly this arises when some among a group of shareholders want an exit. A gap exists in the provision of long term finance that would enable those wishing to remain to buy out those anxious to sell.
- 5.91** We need to ensure that those businesses that want to grow organically without giving up equity have access to the financing options that allow them to do this. In this way we may encourage more business owners to set their growth ambitions higher.

Recommendation 72: Government should ensure the availability of long term patient loan capital to growing businesses which do not want to dilute their equity. It should give serious consideration to tasking the new Business Bank to provide this either by itself or in partnership with the Business Growth Fund.

Improving the quality of demand for finance

- 5.92** Some of the difficulties businesses have in accessing finance are because the loan proposition is fundamentally unsound, or that the case, whilst sound in itself, is not well articulated. It certainly seems the case that too few businesses have the skills to make them appear attractive to banks and other external investors. Only 23% of those responsible for making finance decisions in SMEs have financial qualifications or any financial training⁸⁶. Alongside this lack of in-house expertise, there is also a reluctance to source external advice. Only 9% of SMEs sought advice when seeking an overdraft and only 16% of those seeking a bank loan.
- 5.93** This approach might have worked under the more benign credit conditions which prevailed pre-2008, but it is not good enough in the current climate. More needs to be done to improve the quality of the demand for finance. I strongly support the work that Lord Young is doing to help companies improve their investment readiness as part of his work for government on small businesses. This is one of the areas where chambers of commerce, as partners of the LEPs, could play an important role in ensuring that businesses have easier access advice on preparing loan applications at local level. Chambers will also be well placed to facilitate links between businesses and local banking and investment communities.

Relationship banking

- 5.94** One of the advantages claimed for the ICFC was its capacity to build relationships with businesses at local level and its ability to assess loan applications on their merits. There are widespread concerns that the demise of relationship banking has led to the general loss of this capacity. The quality of loan applications from businesses certainly needs

⁸⁶ SME Finance Monitor Q4 2011

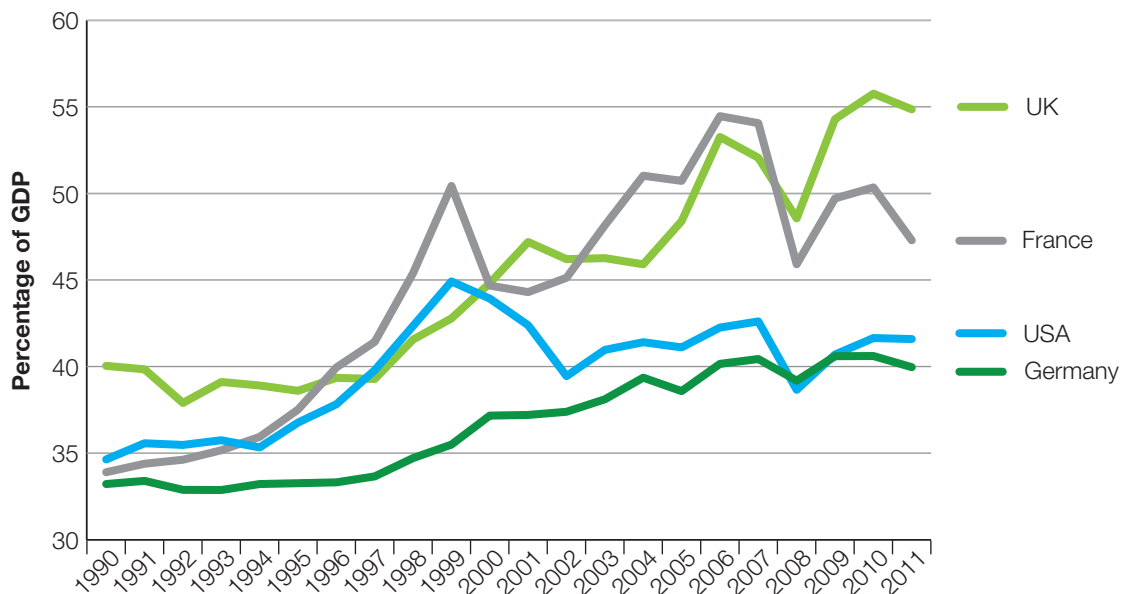
improvement, but there is also a need for banks to enhance their knowledge of business customers, so that lending decisions are taken on an informed basis. There is widespread awareness in the banking world of the need to revive relationship banking capabilities.

5.95 It is encouraging that some banks are taking steps to restore relationship banking. The Swedish bank Handelsbanken is often cited as leading the way. Others need to follow suit. Relationship banking is, of course, resource intensive, but as Handelsbanken can boast, it has had a lower loan loss ratio than its competitors. It can be a viable business model. More needs to be done, but I am hopeful that the introduction of more competition into the market for finance providers will accelerate the trend because it is what the business customer wants and needs.

Foreign ownership

5.96 The UK has one of the most open economies in the world. As the Prime Minister has previously said⁸⁷, ‘we are an open, global economy. There is no protectionist party in Britain. We cannot start creating ownership barriers, trade barriers and protectionist barriers.’ Openness to trade and investment has been a cornerstone of our economic policy for generations and we are heavily reliant on both inward and outward investment.

Chart 5.5: Stock of inward direct investment represented as % of GDP



Source: BIS analysis using UNCTAD data⁸⁸

5.97 Generally it is a stance that has served us well. Investment overseas has improved our access to markets and new technologies, and repatriated profits have played a part in

87 Speech by David Cameron to business leaders at Brierley Hill, February 2010, Birmingham Mail

88 UNCTAD, *World Investment Report 2012*

correcting our trade imbalances. Foreign inward investors have transformed the performance of parts of our economy such as the automotive and steel sectors. Overseas acquirers of UK businesses are usually buying them for good reasons, because they want to build on the performance and skills base of a successful UK company – not asset strip or run it down. They want to work with UK supply chains. They want to use the UK as a base for exporting to the rest of Europe, or other parts of the world. At the aggregate level, the majority of available research points to foreign direct investment having positive effects on the UK economy.

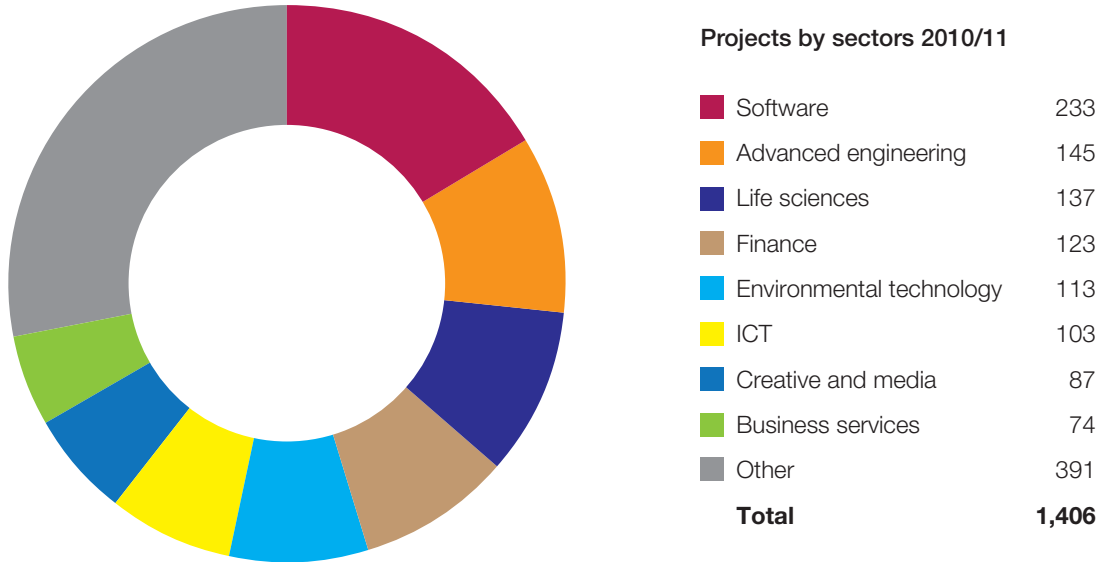
- 5.98** In rare cases, however, an individual transaction can raise concerns connected with its impact on the interests of UK plc. These are concerns which cannot be addressed by the standard test of whether a merger will result in ‘a substantial lessening of competition’⁸⁹. Aside from mergers and acquisitions raising national security and media plurality issues, there is little that successive governments have been prepared to do in these cases. They have left decision-making to the independent competition authorities.
- 5.99** The approach of all British governments can appear disengaged. Foreign investors often ask their lawyers and advisers, ‘what will the UK government think about this takeover?’ They are often surprised to learn that, with very few exceptions, the Government takes no interest in merger activity.
- 5.100** The scale of acquisitions of UK companies, particularly of software, advanced engineering and life science companies is striking. This is not necessarily a bad thing. In some ways it is an indicator of our success in being able to grow new businesses in the high tech sectors. Most acquisitions are entirely unproblematic. However, government needs to have a better sense of how certain types of foreign acquisition might affect our strategic national capabilities.
- 5.101** In today’s world it is difficult to see who else, other than the national government, is capable of looking out for the longer term interests of UK plc. It will not be the asset fund managers whose bonuses are often tied to meeting quarterly performance targets. It will not be the investment funds. As at the beginning of 2012, only about 25% of the top 100 investment funds in the City of London were headed up by a Chief Executive from the UK⁹⁰. Small individual shareholders, who are often more inclined to take a longer term perspective, have no formal means of articulating a collective view, and are increasingly emasculated by nominee accounts. And the directors of the target company must, in practice, often find it difficult to separate their long term view of their company from the personal deals that are offered by the acquirer. Many of these issues were considered in John Kay’s recent, comprehensive work on short termism⁹¹.

⁸⁹ Enterprise Act 2002

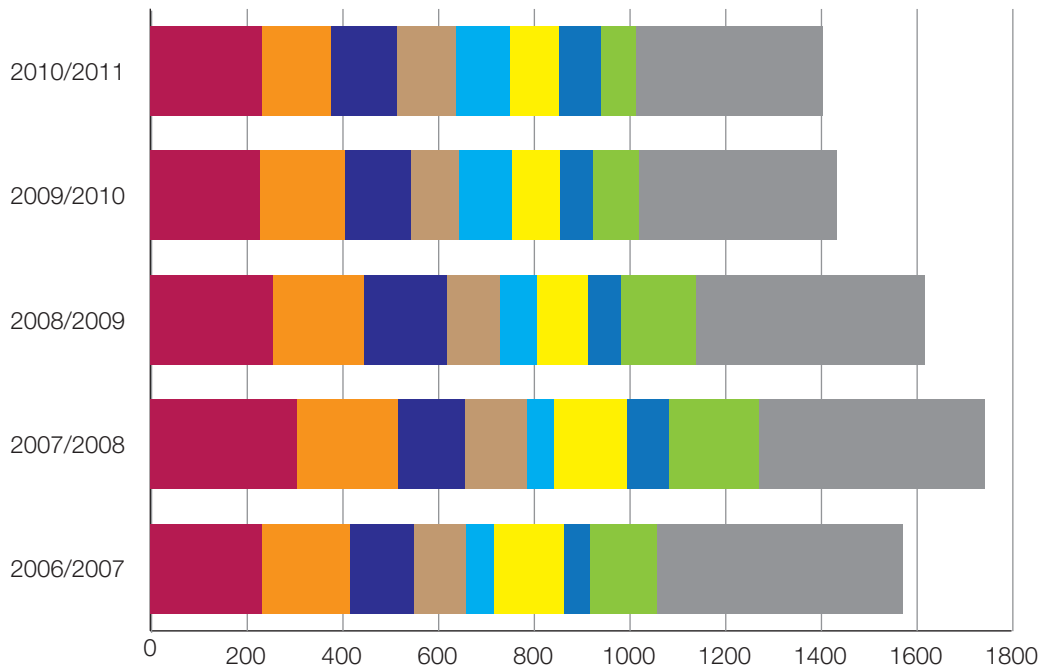
⁹⁰ Unpublished research by Argus Vickers

⁹¹ *The Kay Review of UK Equity Markets and Long-term Decision Making*, July 2012, See in particular pages 58-62. <http://www.bis.gov.uk/assets/biscore/business-law/docs/k/12-917-kay-review-of-equity-markets-final-report.pdf>

Chart 5.6: Inward investment into the UK by sector



Projects by sectors 2006/2007–2010/11



Source: UKTI, Inward Investment Report 2011/12

A way forward

- 5.102** In a global commercial market, we need to preserve and nurture as much added value in the UK as we can, now and for the future. Our R&D capability, intellectual property, advanced manufacturing capabilities and expertise in complex finance and insurance are all vital to the UK's future prosperity. All the major economies with which we compete, such as the US, the French, the Australian and the emerging countries have, in one form or another, powers to protect fundamental national interests in takeover situations. In fact we have too.
- 5.103** The Enterprise Act 2002 already provides powers for ministers to intervene in mergers raising issues affecting national security and plurality of the media. In addition, ministers have powers to create new 'public interest consideration' gateways. These considerations can be applied, not only to future mergers, but to a current merger situation.

Extract from Enterprise Act 2002 – section 42

42. Intervention by Secretary of State in certain **public interest** cases

- (2) The Secretary of State may give a notice to the OFT (in this Part 'an intervention notice') if he believes that it is or may be the case that one or more than one public interest consideration is relevant to a consideration of the relevant merger situation concerned.
- (3) For the purposes of this Part a public interest consideration is a consideration which, at the time of the giving of the intervention notice concerned, is specified in section 58 or is not so specified but, in the opinion of the Secretary of State, ought to be so specified.

- 5.104** The powers have been used just once since the Act was passed. That was to introduce a public interest consideration allowing ministers to intervene in mergers and acquisitions affecting the stability of the financial system. In fact it was put in place, not to block a merger, but to allow Lloyds TSB's takeover of HBOS in 2008 to proceed when it might otherwise have fallen foul of the competition authorities.
- 5.105** Government should show a readiness to use these powers when vital national interests are at stake.
- 5.106** These instances, of course, will be rare and exceptional. What will be far more common are foreign takeovers where UK plc could get far more from the deal than it currently does. Successive UK governments have been too timid in engaging with potential investors in our key sectors to ensure we get the best possible investment in the UK's long term capabilities. We already have many foreign investors adding significant value, building UK R&D capability, developing our domestic supply chains, and developing the skills base.

The Government needs to exert its influence to ensure that more investors make similar commitments, and where necessary make them binding.

- 5.107** Implementing the recommendations I make in Chapter 3 will radically strengthen the links between government and industry. They will involve the establishment of joint industry councils, strengthened sector teams, a streamlined dialogue with trade associations, civil servants with genuine knowledge of sectors and better links with strategically important companies. All this will put government in a much better position to identify strategically important takeovers, and to engage assertively and knowledgeably with foreign investors to secure the commitments that will strengthen our industrial base.
- 5.108** Signalling a greater willingness to use the Enterprise Act powers will help to underpin the Government's negotiating efforts. We would hope the Government never had to use the powers. Their very existence may be enough.
- 5.109** It will be claimed by some that to threaten to use our legislative powers in this way would be to provoke indignation and protest, and would harm the flow of investment to the UK. I reject this. From my knowledge, all leading countries have powers to protect their interests and are prepared to use them, and would expect others to do likewise. Australia, for example, has a review board which assesses proposed foreign takeovers to ensure that they are in the national interest⁹². France assesses mergers against a general interest test which includes consideration of the competitiveness of French companies on the international stage.
- 5.110** Even that bastion of free markets, the US, allows for scrutiny of foreign investment where there are national security concerns⁹³, and prohibits foreign ownership of more sensitive sectors of the economy outright. Dubai Ports World, for example, felt compelled to divest itself of P&O's US ports operations when it took over P&O following intense pressure. Rupert Murdoch, of course, had to become a US citizen to satisfy the legal requirement that only US citizens were permitted to own US television stations.
- 5.111** I do not understand why it is felt that there will be damaging complaints from equivalent economies because all of them have and use such powers.

Recommendation 73: The Government should take a greater interest in foreign acquisitions from the perspective of the UK's industrial strategy priorities, using an enhanced sector knowledge and expertise. Government should do far more to engage with potential foreign investors in our core sectors to secure commitments to developing the UK research, skills and supply base, and in exceptional cases to discourage unwanted investments. We should underpin this by signalling a greater readiness to use existing powers in the Enterprise Act 2002 to allow ministers to consider takeovers and mergers to ensure our long term industrial capabilities are given proper consideration.

92 Foreign Acquisitions and Takeovers Act 1975

93 Scrutiny is via the Committee on Foreign Investment in the US (CFIUS) which reports directly to the President

Chapter 6:

Education and skills – the foundation for growth and prosperity

- 6.1** It is impossible to overstate the significance of education in its widest sense to the sort of society in which we want to live.
- 6.2** This report owes its origins to the need to create wealth far more effectively so that the quality of life in the UK can continue to be enhanced in the century ahead. As international competition intensifies, society becomes more complex, and technological change accelerates, the health of our economy will come to rely more and more on high levels of educational attainment and the availability of a skilled workforce.
- 6.3** But there is another perspective. The child who leaves school with little or no educational attainment is disadvantaged for life. For the vast majority, there is no way back as standards rise and technology permeates into even the least demanding of jobs. Many of those dependent on the state are elderly or incapacitated, but millions are not. They simply cannot or will not compete for the jobs that are available. For many of them this is a tragedy that, in all advanced societies, must be at the top of the political agenda.
- 6.4** Two secretaries of state are at the forefront of our response – the Education Secretary and the Work and Pensions Secretary. Their analysis is correct; their policies well targeted. Any observations I make are designed to reinforce what they have set out to do.
- 6.5** To compete internationally, our education and skills system needs to be producing young people with the competencies, skills and attitudes that make them ready for work. With these in place, individuals can find employment, and once in jobs, are able to work productively. Our goal must be to ensure that our education and skills levels are up to those of the world’s best and are relevant to the world of work. To achieve this when the rest of the world is itself seeking to drive up its own standards is the unavoidable and permanent challenge.
- 6.6** We are some way from our goal. The OECD’s respected Programme for International Student Assessment (Pisa)⁹⁴ assesses the performance of 15 year olds across the world in numeracy, literacy and science. England is currently no better than the average with the latest assessments ranking us at 28th for maths and 25th for reading.

Table 6.1: UK Rankings in PISA tests

Year	2000	2006	2009
Maths	8th	24th	28th
Reading	7th	17th	25th
Science	4th	7th	8th
<i>Total countries participating⁹⁵</i>	32	57	65

Source: OECD, Programme for International Student Assessment

94 www.oecd.org/pisa

95 The decline in the UK’s position is not as steep as it might initially appear because there have been an increasing number of countries participating in the assessments

- 6.7** Reading and maths are fundamental requirements to succeed in any business or industry. Here as elsewhere, we must strive to be better than the average.

Schools

Raising educational standards

- 6.8** Home support in the early years of a child's life is the essential starting point for later success in education. This is well recognised. In many cases this is now supplemented by some form of pre-school education from three. However, it is necessary to start somewhere, and I have taken schools as my starting point.
- 6.9** The performance of some of our schools is world class, but here as elsewhere, it is vital to look at areas of average and poor performance. Not only do we have a moral obligation to educate our children to their maximum potential, but a competitive economy also needs to utilise its human capital to the full. This requires us to raise our educational performance across the board. It means making sure every child is given the opportunity to succeed in a good school, ensuring that – as a minimum – they enter the world of work with sound literacy, numeracy and other core skills.
- 6.10** We are not yet achieving that basic minimum for many of our school leavers. In 2011, only 60% of pupils achieved at least a grade C in both English and maths at GCSE, and almost one in every 20 pupils in maintained mainstream schools failed to obtain a C grade in any subject.
- 6.11** Of deep concern is that nearly one in four of the working age population are not functionally numerate, and almost one in six do not have functional literacy skills. While it appears from the latest results that we are making progress with students leaving school⁹⁶, there are existing issues with some of those already in the work place, a problem which, having been allowed to develop, will now be difficult to remedy.

Table 6.2: Deficiencies in rates of functional literacy and numeracy in the working age population (England)

	2003	2011
Not functionally literate	16% (5.2 million)	15% (5.1 million)
Not functionally numerate	21% (6.8 million)	24% (8.1 million)

Source: 2011 Skills for Life Survey, Department for Business, Innovation and Skills

96 In 2011 94% of pupils leaving school were functionally literate and numerate, achieving at least a level 1 in English and maths.

- 6.12** These bald statistics matter hugely. To bring them to life, someone not reaching a level of functional literacy or numeracy will struggle to read bus or train timetables, or check their pay and tax on a wage slip. They will struggle with comparing products and services for the best buy, and have difficulties working out a household budget. Translate these weaknesses now into the workplace. In the world of care you need to be able to understand the dosage for a prescription, in the garden the warnings on the poison label or in a shop the numbers on the till. Without basic literacy and numeracy skills we leave a swathe of the population inadequately prepared to support themselves or contribute to society.
- 6.13** Problems with literacy and numeracy are deep seated, and go back many decades. In the UK it began to emerge as a problem at the end of the 19th century when the US and Germany started to threaten our industrial hegemony. Too many generations have been let down by the system, and have not had the start in life that they deserve and the country needs. For as long as we are prepared to tolerate failing schools, we will be storing up problems – economic as well as social – that impose long term tax burdens on the working population.
- 6.14** Today, according to Ofsted, there are still 571 inadequate schools in England – around 2.5% of all maintained schools. Poverty, ethnicity or the social conditions in a school’s catchment area are sometimes used as a justification for sink schools. There is no need for this to be the case. With effective leadership and teaching, good schools can exist everywhere. There is no excuse for failure.

Table 6.3: Ofsted inspection outcomes for maintained schools at their most recent inspection – 30 June 2012 (provisional)

Type of school	Outstanding	Good	Satisfactory	Inadequate	Total
Nursery	227	173	19	1	420
Primary	2,997	8,469	4,840	423	16,729
PRU (Pupil Referral Unit)	67	194	109	15	385
Secondary	829	1,248	963	111	3,151
Special	357	454	169	21	1,001
Total	4,477	10,538	6,100	571	21,686

Source: Ofsted⁹⁷

97 Ofsted, *Maintained school inspections and outcomes for the period 1 April 2012 to 30 June 2012*, www.ofsted.gov.uk/resources/official-statistics-maintained-school-inspections-and-outcomes

- 6.15** Based on the results from summer 2011, there were 1,310 schools below the Government's primary floor standard, and 107 schools below the secondary floor standard⁹⁸. In the context of nearly 22,000 maintained schools, these are relatively small numbers, but every underperforming school is unacceptable because it is failing real children and young people every day. It cannot be assumed that it is only the failing schools that are producing the under-qualified children but this indicates an obvious place to start. Children leaving school with poor qualifications are unlikely ever to make good this deficiency.
- 6.16** There are remedies in place to deal with failing schools. Local authorities have powers to issue warnings to governing bodies and to appoint additional governors. They can also apply to the Secretary of State for consent to appoint Interim Executive Boards to tackle leadership, management and staffing issues.

Powers to deal with failing local authority schools

- The governing body of the school is ultimately responsible for the performance of that school, and the head teacher reports to it.
- Where a school has been rated as inadequate by Ofsted, or where a governing body has failed to comply with the terms of a warning notice issued by the local authority (LA), the LA can require the governors to take specified action, appoint additional governors or apply to the Secretary of State for consent to appoint an Interim Executive Board (IEB) to run the school.
- The Secretary of State can also appoint extra governors or an IEB for any school that is rated as inadequate by Ofsted or has failed to act on a warning notice from its LA.
- The Secretary of State ultimately has the power to direct a local authority to close a school if necessary.

- 6.17** In fact, many schools that are failing are closed and replaced with Sponsored Academies⁹⁹. An Academy Order can be issued when a school is rated inadequate by Ofsted or has not acted on a warning from its local authority. As of September this year, there were 501 such Academies, with another 225 failing schools matched up with appropriate sponsors and scheduled to open shortly. Academies have been shown¹⁰⁰

98 A primary school is below the floor standard if less than 60% of pupils achieve Level 4 in both English and maths at age 11 and they are below the median for the proportion of pupils making expected progress in both English and maths between ages 7 and 11. A secondary school is below the floor standard if less than 40% of pupils achieve at least five grades A⁺-C including English and maths at GCSE and they are below the median for the proportion of pupils making expected progress in both English and maths between ages 11 and 16

99 Academies are publicly-funded independent schools that benefit from greater freedoms to innovate and raise standards. Some will have a sponsor, for instance a business or a university.

100 Attainment at Key Stage 4 by pupils in Academies 2011, DfE.

<https://www.education.gov.uk/publications/eOrderingDownload/DFE-RR223.pdf>

to improve faster than other similar schools, and achieve better results for pupils from deprived backgrounds and with Special Educational Needs. They are an important part of the drive to improve standards across the board.

6.18 Good schools require good teachers. I therefore welcome the steps being taken to bring talented people into the profession who might not otherwise have thought about teaching. The Teach First scheme is a case in point. This scheme trains graduates who obtain at least a 2:1 at degree level, and who may not normally have considered a career in teaching. It then places them in schools in deprived areas. It is a bold and imaginative scheme and it is paying dividends. A recent study¹⁰¹ shows that schools with Teach First teachers have seen pupils' GCSE grades boosted by an average of a third of a grade in every subject. Another welcome development is the relaxation of the regulations governing the qualifications people require to teach in schools, to avoid excluding people with valuable wider experience and skills.

6.19 The Education Secretary is taking bold and determined steps to raise the quality of our schools, and to root out failing schools. He is backed by Michael Wilshaw, the new head of Ofsted, who has himself an impressive record as a head teacher. We are moving in the right direction with greater numbers of good and outstanding schools than in recent years and rising expectations for all schools, not just the small minority of failing schools. Ofsted has removed the 'Satisfactory' category, which is a clear sign that only 'Good' is acceptable, and the rising floor standards mean schools are expected to ensure more pupils have good numeracy and literacy skills by the age of 16.

6.20 I welcome the new structure for Ofsted, which is creating eight regions, each under a regional director, to gather local knowledge about schools and address emerging problems more effectively. This is a positive step, but they also need powers to act on what they find. No one should tolerate failing – or even simply inadequate – schools.

Recommendation 74: All failing schools should be subject to the intervention process forthwith. There should be a clear timetable within which an improvement strategy for each school is agreed, with the education authorities using their powers to intervene if the head teacher and governors fail to act. If local authorities delay, central government should intervene.

Recommendation 75: The regional directors being appointed to lead Ofsted's new regional structure should be given formal powers to act swiftly where they identify problems in local schools.

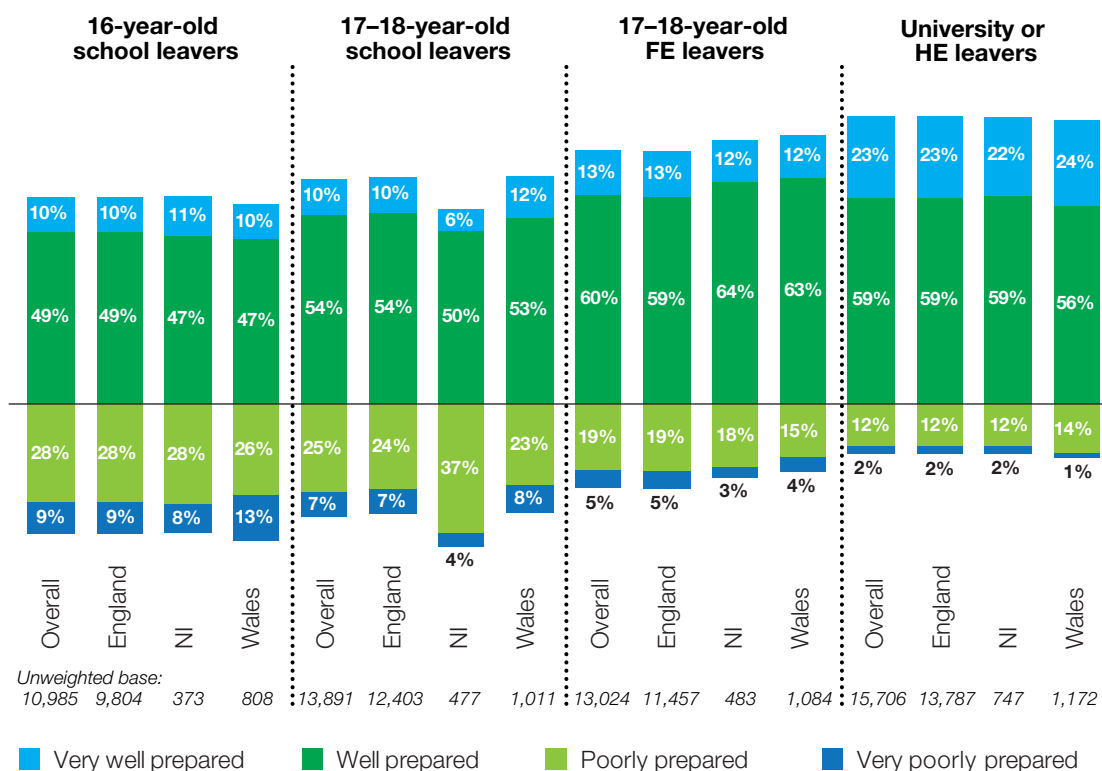
101 *The impact of Teach First teachers in schools*, Manchester University, 2010
http://www.teachforall.org/articles/max_impact.pdf

Improving the employability of school leavers

6.21 Employers complain regularly about shortcomings in the employability of young people leaving school and college. There is now an annual ritual of GCSE results being published accompanied by various surveys from business bodies demonstrating their members' lack of confidence in the readiness of school leavers for the world of work¹⁰². Nothing could illustrate better the gap between what schools are delivering in the classroom and the expectations of employers.

6.22 In a survey of employers carried out by the UK Commission on Employment and Skills (UKCES), 37% of employers said that 16 year old school leavers were poorly or very poorly prepared for the world of work. For 17–18 year olds leaving further education, the equivalent figure was 24%. Better, but with significant room for improvement.

Chart 6.1: Work-readiness of those recruited straight from education in England, Northern Ireland and Wales (2011)



Base: All employers that have recruited each type of education leaver in the previous 2–3 years in England, Northern Ireland and Wales.

Source: UK Commission on Employment and Skills, *Employer Skills Survey 2011: UK Results, 2011*

¹⁰² For an example, see the FSB press notice 'Eight in 10 businesses don't believe school leavers are ready for work and say more should be done to help prepare them for employment'
<http://www.fsb.org.uk/News.aspx?loc=pressroom&rec=7793>

- 6.23** We can increase the employability of young people by educating and enthusing them about the world of work, and demonstrating to them the applicability of what they learn in the classroom. The case study below is an excellent example of teaching our future workforce about the basics of business, proving that you are never too young to learn.

Aylsham High School – enterprise activities

Aylsham High School prides itself on its excellent working partnership with local business, community and feeder schools.

An example of building business awareness from a young age is the day Year 1 children work with their business partners at the farmers market. Each school has its own stall on the day and children as young as five years old start to understand profit and loss, make decisions and communicate with the public.

The students are thoroughly motivated by enterprise. The chairperson of Young Chamber states:

‘Enterprise is brilliant, it takes us in to the real world and helps us to learn skills that we will need for our future’.

- 6.24** I am of the same mind as the Work and Pensions Committee report¹⁰³ that stated that ‘as well as arranging work experience placements where appropriate, schools, in coordination with local employers, should incorporate work-related learning into lessons at Key Stage 4 (14–16 year olds) and for younger school students to provide work-related learning’.
- 6.25** There are many reasons for fostering a greater involvement of business with schools. It is not just a nice to have. Where it is sustained and systematic, it delivers tangible improvements in outcomes for schools. Evidence shows that young people who have experienced employer engagement activities such as work experience, are five times less likely to end up outside education, training or employment¹⁰⁴. Employer involvement in schools can also increase understanding of career opportunities and ensure better and higher quality work experience. It can help students improve their CV writing and interviewing skills in a realistic setting. Crucially, it can help ensure that young people’s decisions about future education and training options are informed by real and early exposure to the business world.

103 *Youth Unemployment and the Youth Contract*, Work and Pensions Committee, 2012,

<http://www.publications.parliament.uk/pa/cm201213/cmselect/cmworpen/151/15102.htm#evidence>

104 Employer and Education Taskforce, *It’s who you meet*, 2012

- 6.26** University Technical Colleges (UTCs)¹⁰⁵ and Studio Schools¹⁰⁶ are an excellent way to bring business and education together and inspire young people. Lessons are delivered in state of the art facilities with clear, real-world applicability. This ensures that students recognise the relevance of what they are learning and how it can help them in their future career. The Academy programme more generally is getting more business leaders involved with education, and has been an effective way of building links between the sectors. We should welcome bids from Local Enterprise Partnerships (LEPs) and their partner organisations for funding to open more UTCs within the single pot framework as well as via existing routes.
- 6.27** If businesses can successfully play a role in improving the standards of some schools, then they should do it in all schools. It is no good having businesses criticising from the side-lines. They need to be playing an active part in improving the employability of young people by engaging fully and effectively with the education system. Employers could be offering a range of services, including work experience, careers advice, work place visits, and inspirational talks from leading local business people. As mentioned in Chapter 5, local chambers of commerce could have an important role to play coordinating this engagement.
- 6.28** Thankfully, we are pushing at an open door. The CBI has found that engagement with secondary schools is a clear priority for employers, with many saying they would be prepared to do more¹⁰⁷. KPMG's Evaluation of Education and Employer Partnerships¹⁰⁸ found that 85% of secondary head teachers believed it was either 'very or extremely beneficial to have a business partnership'. They wanted greater engagement with local employers but were often unsure where to start.
- 6.29** In my own conversations around the country, I have found no shortage of schools keen to engage with business, and businesses keen to engage with schools. There were many examples of excellent school and business partnerships already in place. I learned about organisations such as Business in the Community¹⁰⁹ and Ahead Partnership, who are already facilitating this sort of engagement between schools and employers.

105 UTCs are academies for 14–19 year olds. They focus on providing technical education that meets the needs of employers.

106 Studio Schools are set up with the backing of local businesses and employers. They teach academic and vocational qualifications, with a strong emphasis on work placements.

107 CBI, *Learning to Grow, Education and Skills Survey 2012*

108 KPMG, *Evaluation of Education and Employer Partnerships*, May 2010

109 <http://www.bitc.org.uk/>

Ahead Partnership¹¹⁰ – facilitating school and business partnerships

- School and business partnerships can be difficult to establish and sustain because of the time pressures on both sides.
- Ahead Partnership’s ‘Make the Grade’ programme provides secondary schools and their partner primary schools with bespoke education and business partnerships. A menu of activities allows each school to construct a programme to meet its precise needs.
- Partnerships are structured around a three year initial term, with all the business recruitment, planning and facilitation provided by Ahead Partnership.
- Each partnership is supported by a cross-sector group of committed businesses that engage in activities and help fund the modest facilitation costs. Smaller businesses, public sector and non-profit organisations also engage in activities, bringing further breadth and innovation to the programme.
- The programme launched in Leeds in 2011 and the model is now being extended into the Leeds City Region and other areas.

Recommendation 76: Business engagement should be incorporated far deeper into the school curriculum in order to develop young people’s understanding of business, increase their employability, and further their understanding of career and future training options and where they might lead. LEPs should consider how they engage with local schools and work with chambers to facilitate this.

6.30 In the course of my review, I heard complaints from schools, colleges and employers that the paper work and bureaucracy connected with health and safety risk assessments and Criminal Records Bureau checks are deterring worthwhile activity such as work experience and college placements. I heard suggestions that it ought to be possible for workplaces to be accredited as being fit to receive students and young people. This would remove the need for individual risk assessments for each new placement. These ideas should be looked at seriously. At a time when the Education Department (DfE) is trying to make sure that high quality work experience is available for those aged 16-19, barriers must be streamlined or removed.

Recommendation 77: The bureaucracy and paper work around work experience and work placements must be streamlined. DfE must be clear about what is absolutely necessary. Government must then ensure the removal of all regulations and requirements that place unnecessary burdens on employers, schools and colleges.

¹¹⁰ Ahead Partnership started in Leeds in 2004 and now operates across the UK, bringing the private sector together with public and third sector organisations to deliver projects that unlock social and economic potential. Ahead Partnership is a non-profit distributing company.

6.31 Engagement between employers and schools could also be enhanced by increasing the number of employers on the boards of governors of schools. They bring with them expertise and a perspective that other governors may not have and schools welcome their presence and insight. They have links with other employers, and can be a catalyst for wider engagement with the business community.

Recommendation 78: All boards of governors in secondary schools should include two influential local employers, at least one of whom should have good connections with the wider business community. This could be coordinated by the local chambers of commerce.

Improving the incentives on schools to prioritise employability

6.32 Is it surprising that so little of the school day is spent preparing pupils for employment? Whilst we continue to judge schools solely by the number of pupils achieving A*-C grades the focus on what happens afterwards is inevitably reduced. The incentive is to teach for tests, not ensure a set of skills valued by the local economy and employers. Employers are clear that when assessing future potential, they rate attitude and personality (91%) and work experience (55%) as more important than educational attainment (35%)¹¹¹.

6.33 Currently, there is more incentive for the school to move the marginal D grade maths pupil to a C than there is to make sure that the pupil has the best chance of gaining employment, either directly or through further education or training. We must start putting more emphasis on the outcome from academic learning, rather than simply measuring the number of qualifications.

6.34 I am encouraged by two developments. First, the Department for Education has recently published the first ever 'Destination Measures' index¹¹². This tracks where pupils go after leaving school and provides a robust indicator of how successful schools are in getting their leavers into employment, training or further academic study.

6.35 Second, from September 2012, Ofsted assessments will look at the support a school provides to prepare pupils for the next stage in their lives, whether it be to further academia, vocational training, or the local labour market. I welcome and support this development.

Recommendation 79: Local authorities should publish the Destination Measures for all secondary schools in their areas alongside academic attainment so that parents can make better informed choices, and to incentivise schools to give a higher priority to developing the employability of their leavers.

¹¹¹ Adecco Group, *Unlocking Britain's Potential*, 2012

¹¹² <http://www.education.gov.uk/childrenandyoungpeople/youngpeople/participation/a00208218/key-stage-4-and-key-stage-5-destination-measures>

Careers advice

- 6.36** To give our young people the best possible chance of a successful career, we must make them informed learners. Careers advice is vital and I believe that this needs a much more localised focus.
- 6.37** Research studies suggest that young people particularly value information on jobs and careers if obtained in a real workplace and through contacts with working people¹¹³. Through such experience young people can be better prepared to make the education and training decisions that will shape their future career paths.
- 6.38** The Government's recently launched National Careers Service is suitable for providing a high level national perspective and information relating to sectors. However, a centralised system like this is not a substitute for good on the ground advice with sound local knowledge. I agree with the recent Work and Pensions Committee report¹¹⁴ which found that the 'National Careers Service offer of online and telephone advice to younger students is not an adequate alternative to face-to-face careers guidance'.

Recommendation 80: The existing budget lines for adult careers advice should be included in the single funding pot. Each LEP, as part of its local economic plan, should consider how careers advice is best provided in its area to meet the needs of both the adult population and the requirement under the Education Act 2011 for careers advice in schools.

Further education, vocational training and apprenticeships

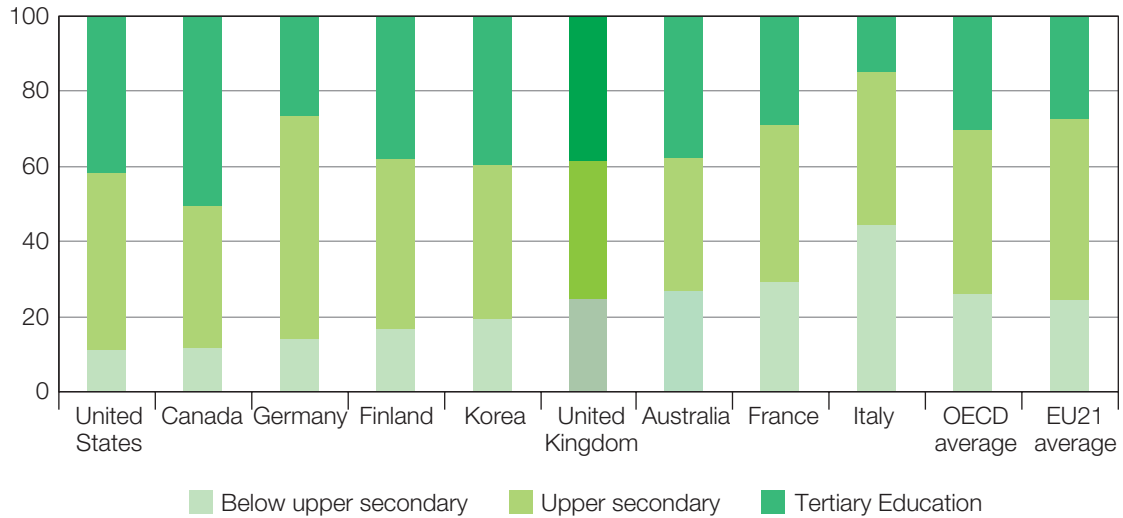
- 6.39** It is essential that young people leave school with the basic competencies in place to progress into the workplace, or into further education and training. They then need to acquire the more specific skills required by employers. International comparisons show that we have a long tail of adults holding only very low level qualifications with not enough of our students reaching at least upper secondary level (equivalent to 5A*-C GCSE grades). This is despite our relatively good performance on the numbers of young people reaching university level.

113 OECD, *Learning for Jobs: Synthesis report of the OECD reviews of vocational education and training*, 2010

114 *Work and Pensions Committee, Youth Unemployment and the Youth Contract*, 2012,

<http://www.publications.parliament.uk/pa/cm201213/cmselect/cmworpen/151/15102.htm#evidence>

Chart 6.2: International comparison of workforce qualifications amongst the population aged 25–64



Source: OECD, Education at a Glance 2012

6.40 The following case study shows how the US develops a curriculum to meet local manufacturers’ needs and aligns the provision of intermediate level skills in order to deliver economic growth and jobs.

US approaches to developing intermediate skills¹¹⁵

The US President’s Council of Advisors on Science and Technology refer to community college level education as the ‘sweet spot’ for reducing the skills gap in advanced manufacturing and recommend increased investment as well as the development of business and educator partnerships to provide skills certifications and accreditation. These will underpin the development of location specific curricula to meet the needs of local manufacturers.

The Chicago area is a good example of where the transformation of the City College system to address gaps at the mid-skill level is an integral part of the City Mayor’s plan for Economic Growth and Jobs. Six campuses will focus individually on a different industrial sector and skills set with local employers actively engaged in curricula design.

6.41 Government rightly funds a wide range of education and training for 16-19 year olds and adult learners, as well as capital maintenance of educational establishments.

115 Report to the President on Capturing Domestic Competitive Advantage in Advanced Manufacturing, President’s Council of Advisors on Science and Technology, July 2012

- 6.42** The Department for Education funds learners up to the age of 19 via the Education Funding Agency. Funding for adult further education and skills training in England is administered by the Skills Funding Agency (SFA), an agency of the Business Department. The allocated budget in 2011/12 for the SFA totalled almost £4 billion, of which £2.8 billion was spent on adult skills.
- 6.43** The SFA's work is particularly challenging and complex. It deals with a highly diverse range of training providers, from Further Education (FE) colleges through to private sector companies. The ultimate beneficiaries of the funding are also diverse, ranging from people who have left the education system without basic qualifications who need to acquire basic skills, through to individuals on apprenticeship training schemes, or studying for high level vocational qualifications.

Deficiencies in the current skills system

- 6.44** Unfortunately, as a whole, the system is not delivering what the economy needs.
- > The current system does not incentivise FE providers to run the courses that deliver the greatest economic benefit. For example, within the apprenticeships programme, the vast majority of the recent expansion has involved apprentices over 25 (who now account for over 40% of the programme) and who are already in work with their employer¹¹⁶. The evidence¹¹⁷, however, suggests that it is investment in younger individuals starting an apprenticeship as a new job which has a greater economic impact.
 - > In most instances, skills funding flows to the courses that students demand and which colleges can fill. It is hardly surprising then, that there is often a mismatch between the skills being taught and the skills that employers are demanding or the jobs likely to be on offer. This either results in employers needing to retrain students, or not being able to fill vacancies. The press has seized on the oversupply of hairdressers, where we trained 94,000 students in 2010/11 for an industry where there are only 208,000 employed, and only 18,000 vacancies. In contrast, only 40,000 students trained in building services engineering when there were nearly double the number of job vacancies in that sector¹¹⁸. Whilst the report from which this data is taken acknowledges data limitations, it is a story I have heard repeatedly and is illustrative of a fundamental problem.

116 http://www.thedataservice.org.uk/NR/rdonlyres/75CE17E4-2DAA-475F-80F9-CA9178D20946/0/SFR_commentary_October_2012.pdf

117 BIS Research Paper No. 76: *Evaluation of Apprenticeships: Learners*
<http://www.bis.gov.uk/assets/biscore/further-education-skills/docs/e/12-812-evaluation-of-apprenticeships-learners.pdf>

118 Centre for Economic and Social Inclusion, *Hidden Talents: Skills Mismatch Analysis*, June 2012

Table 6.4: FE and skills achievements¹¹⁹ by occupation/sector compared to actual number of vacancies (England 2010/11)

Sector	FE and skills achievements	Vacancies	Vacancies per skills achievement
Automotive industries	36,800	89,017	2.4
Building services engineering (electrotechnical, plumbing, etc.)	39,740	71,789	1.8
Construction	123,370	273,969	2.2
Creative and cultural industries	82,950	65,672	0.8
Hair and beauty	94,420	18,016	0.2
Hospitality, leisure, travel and tourism	97,910	43,174	0.4

Source: Centre for Economic and Social Inclusion¹²⁰

- At present, there is little incentive for training providers to adapt their offer to meet what the economy needs. The majority of funding comes from the SFA, not the employer or learner. In 2010/11, for example, total FE college income was more than £7.5 billion, of which only 2% was fee income from employers¹²¹. What this means is that providers are able to pick and choose what training to deliver, and employers are often unaware of the quality, relevance or benefit of the training being provided.
- The system does not do enough to attract private investment in vocational training. Government funding for skills is falling by around 25% over the Spending Review period. That is an inevitable consequence of the Government's deficit reduction programme. Overall spending on skills, however, needs to increase significantly if the UK is to maintain or improve its position relative to competitors in the OECD. The only way of squaring this circle is for government to be more effective in using its reduced contribution to leverage in larger contributions from employers and individuals. Loans will do this to a limited extent for individuals at higher levels, but more is needed.

6.45 The following chart provides a stark illustration of perceived problems with the quality of our vocational education and training (VET) system¹²². It is based on a survey of multi-national companies and experts and suggests that we have a system that lags a long way behind two of our peers. Out of a maximum score of ten, nearly 50% of respondents gave Britain an overall score of five or less for the quality of our VET system.

119 FE and skills achievements in this data include intermediate and higher/advanced level apprenticeships, education and training at levels 2 and 3 (excluding skills for life), and workplace learning

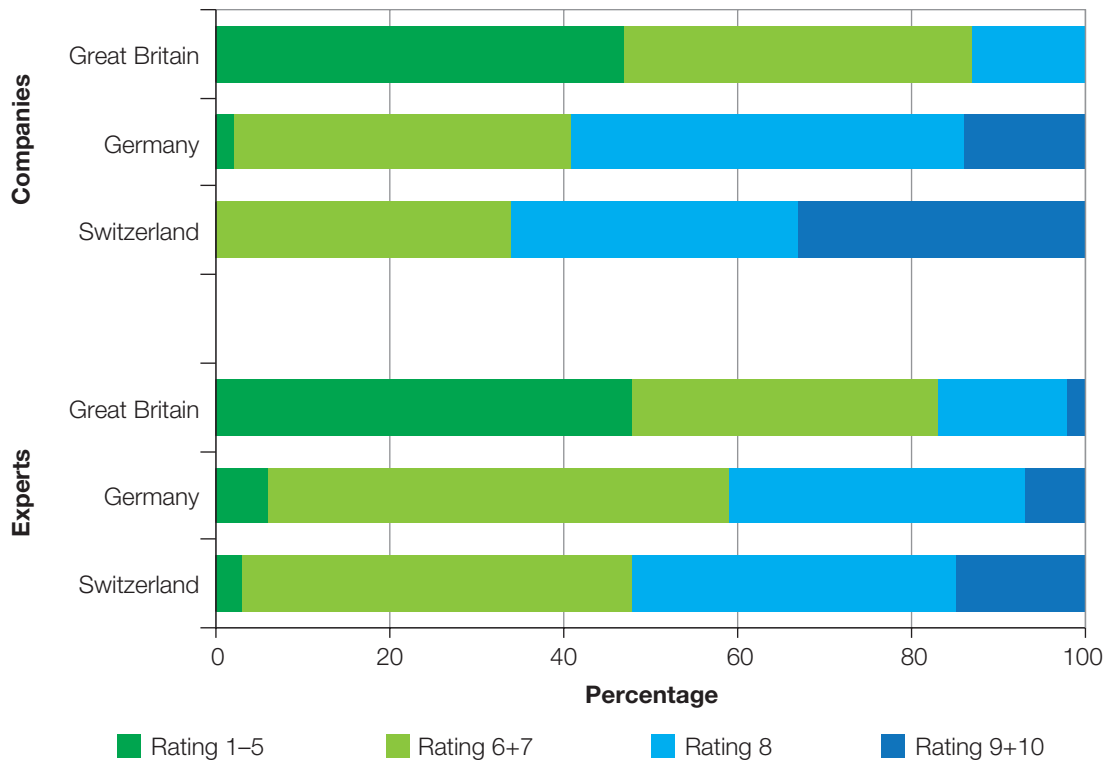
120 Centre for Economic and Social Inclusion, *Hidden Talents: Skills Mismatch Analysis*, June 2012

121 *Analysis of College Finance Records for 2010/11*,

<http://skillsfundingagency.bis.gov.uk/providers/finance/financialmanagement/financialmanagement/collegeaccounts/>

122 VET, *A competitive and decisive factor for Switzerland*, Federal Office for Professional Education and Technology, Swiss Confederation, 2011

Chart 6.3: Comparative ratings of vocational education systems in Britain, Germany and Switzerland (2011)



Source: Federal Office for Professional Education and Technology OPET, Swiss Confederation

Making the skills system more responsive to local employer needs

6.46 Some steps have been taken to make the skills system more responsive to employers' needs and the local demand for skills, and to leverage in additional funding.

- The Employer Ownership Pilot invites employers to bid for up to £250 million of contestable public investment over two years. The pilot incentivises employers to develop skills solutions which achieve economic value, leverage better employment and workforce development outcomes, and help industries and localities to secure the future capacity and capability required for growth. By routing funding through employers, the pilot also supports a genuine market in which employers negotiate with providers to procure training that meets their needs at a competitive price. The pilot programme has already identified innovative approaches that work at both the national/sectoral level as well as at the local level. The second round of the pilot is an opportunity to build on this approach as an interim step towards the LEP-led strategies I envisage by looking to employers to take the lead – in partnership with LEPs and colleges – in developing and delivering the vocational training needed to grow their local economies.

- Several of the recently announced City Deals include agreements for devolving responsibility for skills. Sheffield City Region, for example, is developing a local skills funding model to address skills gaps in key sectors such as advanced manufacturing. It plans to lever in £44 million of local and private sector investment in return for £28 million of devolved funding from central government. Leeds City Region is also seeking greater influence over the skills system through its Employment and Skills Board which will ensure that investment goes into the skills that the local economy needs.

Devolution of the skills budget

- 6.47** These are steps in the right direction, but they are nowhere near comprehensive or far reaching enough. We are not going to succeed in aligning the skills system with the needs of local economies without devolving a significant proportion of the central skills funding to local areas, and allowing business a far stronger influence in what is provided.

Recommendation 81: The budget for vocational training for learners aged 19 and over, and all funding currently set aside for apprenticeships for those aged 16 and over, should be devolved to local areas through the single funding pot described in Chapter 2. This therefore calls into question the continuation of the Skills Funding Agency. Each LEP should incorporate skills needs within their local economic plans driven by the needs of local employers and the practical experience of FE colleges.

- 6.48** Some will question why I have not included the funding for vocational training for 16-18 year olds, other than apprenticeship funding. The Government, through increasing the participation age to 18, is sending a clear signal that young people should be in continued learning until this age and I agree that this should remain funded through the Education Funding Agency to achieve this target. I am also aware that the type of learning undertaken by 16-18 year olds is often less specialised, and students at that age need to acquire a greater breadth of knowledge than would perhaps be prioritised by business. However, we should ensure that the courses that are studied are relevant, lead to qualifications that businesses value, and ultimately lead to jobs. We must not allow the situation to develop that I have outlined above where skills do not meet local labour market requirements.

Recommendation 82: All FE learning providers must consult and agree their provision with LEPs to ensure that the courses they offer to 16-18 year olds reflect local labour market requirements. In addition, any vocational courses delivered by FE providers to learners of any age must conform to the defined national standards set by employers and industry.

Addressing the practicalities of a devolved skills system

- 6.49** The plans will be for local areas to develop, but I envisage the chambers of commerce playing an increasingly important role alongside the LEP in defining and articulating the skills needs of local businesses. I also envisage them aggregating the demand from smaller employers for particular types of training and then negotiating with FE colleges and other local providers, including companies, to ensure that the demand is met.
- 6.50** LEP plans will also need to reflect the practical experience of FE colleges in delivering the courses that underpin the core needs of the local community in conjunction with the strategic needs of local priority sectors as set out by the LEP. These plans will need to be creative in finding ways to use public money to unlock additional investment in skills.
- 6.51** Adults without basic qualifications currently have a statutory entitlement to remedial training in literacy and numeracy. My proposals do not affect these and other statutory entitlements to skills training. LEP plans will need to say how they intend to address these statutory entitlements.
- 6.52** I envisage the Industry Councils playing a key role in articulating the national skills needs for the sectors they represent and feeding this information into the national growth strategy. It will then be for LEPs to originate proposals with the help of Local Growth Teams to contribute to this national requirement. The Local Growth Teams will work with the Government's sector teams to ensure that aggregate needs are met.
- 6.53** There is universal agreement that all apprenticeships must be of good quality, with national standards and branding, and aligned with the skills and knowledge which employers need. It is essential that qualifications are rigorous and transferable. I envisage these being defined and accredited at a national level by industry, such as through Industry Councils.
- 6.54** I believe that apprenticeships should be routed primarily through the local model I have outlined in order to ensure that they meet the needs of local employers, including SMEs. Relatively few small businesses currently offer apprenticeships¹²³ but local coordination aimed at stimulating supply and demand for apprenticeships should start to address this.
- 6.55** In the vast majority of instances there will be advantages to both small and large employers in being able to articulate their skills needs in a local context. Employers will be able to discuss their requirements with one or – at most – a small number of LEPs. However, in the limited case of large, nationally spread employers such as British Telecom, an alternative route to funding will need to be found as it would be unreasonable to expect them to deal with a large number of LEPs.
- 6.56** Some critics will say that this local partnership approach is unrealistic. It is, however, commonplace in other countries. Switzerland provides an example of how it can be achieved.

123 Jason Holt, *Making apprenticeships more accessible to Small and Mid Sized Enterprises*, 2012 and UKCES, National Employer Skills Survey, 2009

Vocational training in Switzerland

Vocational training is a popular option for young Swiss people (two thirds opt into it) and it enjoys a high level of business engagement. Employers are culturally committed to up-skilling their staff and contributing to the wider training system. Roughly one third of the companies in Switzerland engage in the apprenticeship programme. Most vocational education and training (VET) programmes consist of part time classroom instruction at a VET school combined with a part time apprenticeship at a host company. There are around 230 occupations to choose from.

The Swiss system is a collaborative partnership model involving the federal government, the Cantons (provincial government) and trade associations.

- The Federal Office for Professional Education and Technology ensures quality and strategic planning and development of the VET system.
- The 26 Cantons implement and supervise training programmes. They are responsible for vocational school and work-based training, provide career guidance and inspect host companies and industry training centres.
- Trade associations and other professional bodies are responsible for the training content and national qualification procedures.

The apprenticeship system is determined by a combination of the availability of training places in companies and students' preferences. In order to start their apprenticeship students need first of all to find a vacancy in a company and sign a contract. A place in a vocational school is then automatic.

The Cantonal VET offices play an important role. These offices are familiar with the conditions in their regions and are therefore well placed to establish and maintain contacts with local businesses. They assess the number of available apprenticeships, encourage local businesses to offer an apprenticeship position, and offer individual support to young people in their search for an apprenticeship position and subsequent mentoring.

The close connection to business and employers ensures a strong focus on career guidance throughout the apprenticeship process.

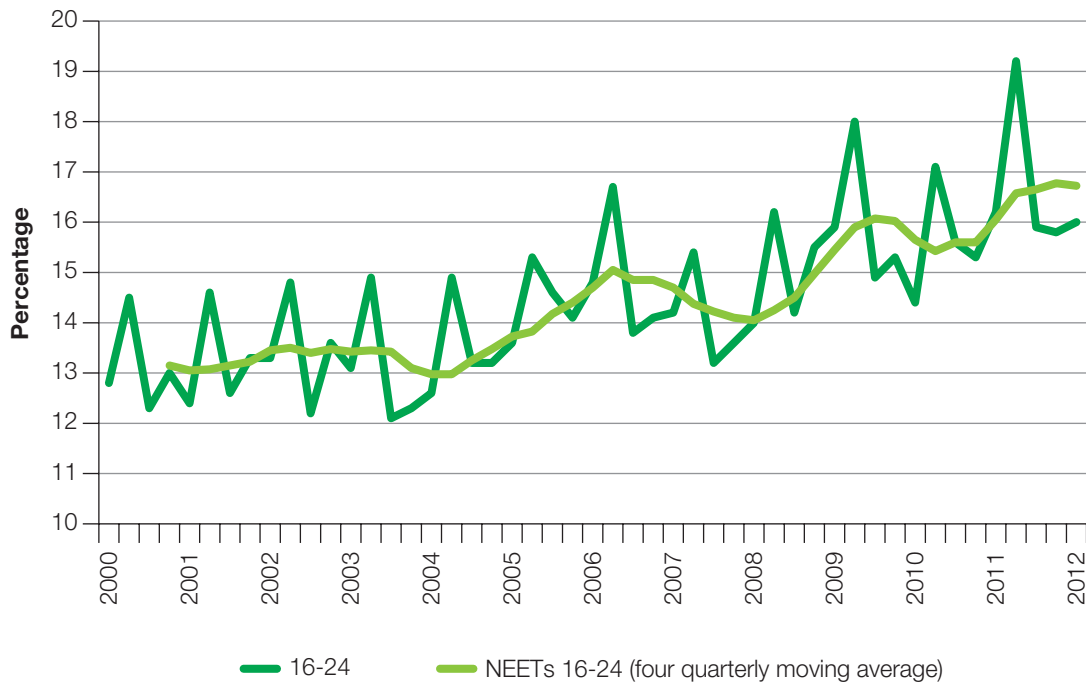
- 6.57** To avoid businesses re-classifying existing employees as apprentices, and to ensure genuine additionality in the system, we could adapt the Swiss model where the local offices work closely with employers to assess the number of available apprenticeships and ensure their quality and validity. In our case, this would be a role for LEPs and the chambers.

Those not in education, employment or training

6.58 An increasing proportion of our young people find themselves not in education, employment or training (NEET). My recommendations so far will tackle the problem at source by providing better educational foundations, better local career information and guidance, inspiring young people with the world of work and by directing skills budgets to where there are job opportunities.

6.59 However, we must also act on the existing pool of NEETs as even relatively short spells of unemployment can lead to prolonged and even permanent effects on earnings and well-being¹²⁴.

Chart 6.4: Percentage of young people not in employment education or training in England



Source: BIS analysis based on data from The Data Service and DfE¹²⁵

6.60 Local authorities and LEPs have a key leadership role to champion the interests of all young people in their area. They will be working with providers, employers, local voluntary and community organisations and neighbouring authorities to raise achievement, secure access to high quality provision and raise participation rates.

6.61 An example of a multi agency approach at a local level was the Prolific and Priority Offender Scheme. This brought together a range of public, private and third sector

¹²⁴ Paul Gregg and Emma Tominey, *The Wage Scar from Youth Unemployment*, CMPO, 2004, University of Bristol. This report found the impact of six months of youth unemployment led to wages 13-21% lower nearly twenty years later

¹²⁵ http://www.thedataservice.org.uk/statistics/statisticalfirstrelease/sfr_supplementary-tables/neet/ and <http://www.education.gov.uk/rsgateway/DB/STR/d001082/index.shtml>

organisations to reduce re-offending amongst prolific offenders. The programme successfully reduced re-offending by 43% and demonstrates how combining local resources can have a significant impact on entrenched problems¹²⁶.

- 6.62** A similar approach would be effective in addressing the problem of NEETs. The problem is a local one affecting local communities. All the organisations with a part to play in finding solutions are local, including the schools from which the young people emerge, the advisers in the benefits office, the local employers and training providers, local authorities and a myriad of charities and social enterprises. The expertise and local knowledge is all present. What is needed is a catalyst to bring the local agents together to develop creative and tailored local solutions.
- 6.63** The City Deals have provided just such a catalyst. The recently concluded deals for Leeds, Liverpool and Newcastle all include locally-developed ideas for tackling youth unemployment. Action to tackle NEETs is, in fact, the cornerstone of the Leeds City Deal. There are currently about 47,000 people under the age of 25 in the Leeds region who fall into the NEET category which is a serious constraint on the economic potential of the area. The region's response has been the development of a "Guarantee for the Young" – a comprehensive approach to tackling the problem.

Leeds City Region – Guarantee for the Young

Leeds City Region is offering a new 'Guarantee to Young People' – a commitment that every young person in the Leeds City Region will have access to a job, training, apprenticeship, volunteering or work experience.

This offer is being supported by:

- a locally designed youth employment model that will create 20,000 new opportunities for young people
- an innovative 14–24 Academy that will deliver a business led curriculum
- an Apprenticeship Training Agency which will support small businesses that have traditionally shied away from apprenticeships because of costs or bureaucracy
- a wider apprenticeship brokerage service to link young people and employers
- piloting a local alternative to the national youth contract for 16–17-year-olds.

In addition, the region will get greater influence over the skills system through an Employment and Skills Board which will ensure that investment goes into the skills that the local economy needs.

¹²⁶ Home Office, *An impact assessment of the Prolific and other Priority Offender Programme*, Paul Dawson and Lucy Cuppleditch, Home Office Online Report 08/07

Recommendation 83: Action to address NEETs is best taken at the local level. Resources to tackle the problem should therefore be available from the single pot. Youth unemployment will not be a problem or priority for action in every area, but where it is, LEPs working with local authorities, employers and other local partners should develop proposals for reducing NEET numbers as part of their local economic plans.

Social deprivation

- 6.64** In a review centred on growth, some might question whether I should address the issues of social deprivation and long term unemployment. But to my mind, they are interwoven. The costs have to be met and thus resources diverted. Finding a way to get people into employment is life enhancing for them and socially desirable for the community at large. To tackle this problem and with it the existence of the forgotten people of the sink estates should be central to political purpose and helping our economy to grow.
- 6.65** In the work that the Work and Pensions Secretary is developing and planning to extend significantly next year, I would suggest that he will be materially helped if he can embrace the wider resources of each local community. Deprivation is a much wider phenomenon than worklessness. Many law enforcement agencies and local government employees in areas such as care deal with these issues every day. In driving forward the new agenda, I believe that the prospect of successful outcomes would be greatly enhanced if existing responsible bodies were more closely co-opted into the important work that lies ahead. I was impressed, for example, by the offer of the new Mayor of Liverpool to develop such a concept.

Higher Education

- 6.66** Achieving a degree remains one of the best ways of securing a good job with long term prospects for a rewarding career. Demand for graduate employees continues to increase, with forecasts suggesting that graduate jobs will constitute half of all job vacancies arising this decade.
- 6.67** The number of graduates across the world has been increasing year on year, a trend which will only continue as more and more developing countries invest in their higher education systems. In order to remain competitive it is vital we continue to produce graduates of the highest quality who can drive growth by increasing productivity.
- 6.68** Professor Sir Tim Wilson undertook a thorough review¹²⁷ of collaboration between the business and university sectors, which was published in February 2012. I am grateful that I have not had to re-examine that evidence in greater depth, and can instead reinforce Professor Wilson's well considered recommendations in the area of graduate employability and skills.

127 Tim Wilson, *A Review of Business University Collaboration*, 2012

- 6.69** Professor Wilson identified work experience opportunities and employability skills for graduates as key enablers that allow students to move smoothly from university into a business environment. He also highlighted the importance of business involvement in programme delivery, design and sponsorship in ensuring students leave higher education with skills that are of real value to employers. This will ensure that graduates can begin making a valuable contribution to growth after only a minimal transitional period.
- 6.70** This government is moving towards a more market-based system in higher education. For a market system to be efficient, information is key. Students must know that what they are paying for will stand them in good stead for the long term. There are too many stories of students completing courses which are not relevant for today's jobs, let alone tomorrow's. The days when the teacher in Evelyn Waugh's short story, Scott-King's *Modern Europe*¹²⁸ could say, 'it would be very wicked indeed to do anything to fit a boy for the modern world' are long gone.
- 6.71** I welcome the Government's introduction of Key Information Sets, which will make valuable information, like employability statistics, available to prospective students to allow them to make a more informed choice of course. I also applaud the development of kite-marking for degree courses. For instance Skillsset, the Sector Skills Council for the creative industries, has introduced a scheme called 'Pick the Tick' which provides information about which degree programmes have been endorsed by employers.
- 6.72** Courses must increasingly be developed wherever appropriate in collaboration with industry so that we no longer get into the situation where students complete courses which employers in that sector do not value. Employers must also facilitate work placements for learners in order to develop the applicability of what they are learning.

Recommendation 84: Industry Councils should work with the higher education sector to ensure that courses are relevant, incorporate placements in industry, and match the skills for which there is demand. Government needs to consider incentives to encourage and develop this further.

- 6.73** Businesses can also play a more direct role. Those businesses that are prepared to pay a proportion of students' course fees will be able to exert influence over the course content and delivery and help ensure graduates are work ready. They will also have the incentive to ensure that they do all they can to ensure that the education received is of the very best standard and relevance by providing work based learning.
- 6.74** Following the Leitch Review of Skills in 2006, the Higher Education Funding Council for England (HEFCE) sought to develop a new model of co-funding with employers. A Workforce Development Programme invested over £150 million over 2008–2011 in universities to develop their operations with employers around this co-funding model, with the aim of producing 35,000 new workforce entrants by 2011.

128 Evelyn Waugh, *Scott-King's Modern Europe*, 1947

- 6.75** The programme enabled universities to leverage around £38 million investment from employers and to provide additional places for students outside specified quotas. I understand the programme was successful in providing a platform of capability and capacity for workforce development within the HE sector. As a consequence of the Government's HE reforms, HEFCE will no longer directly fund courses; nevertheless, I would encourage businesses to continue to co-finance student places.
- 6.76** Universities and employers should develop a model where a commitment from firms of between a third and a half of a student's course fees will commit the student to working for that employer for a fixed number of years after graduation. This will bring benefits to all parties. The university will be able to accept students above their standard quota and so gain additional income; the student will know that the course is valued by employers, and that they have the guarantee of employment once qualified; and the employer will know that they will be recruiting a graduate with the skills and knowledge they require.
- 6.77** This approach is likely to be particularly valuable in the STEM (science, technology, engineering, and mathematics) sectors where there remain concerns that there will be a shortfall of graduates in filling the anticipated vacancies. It is estimated¹²⁹ that there will be a requirement for more than 100,000 STEM graduates per annum for the period 2012–2020 and that this will not be met by newly graduating STEM students who currently number only about 90,000 per year. The gap will, in fact, be wider than this because a significant proportion of STEM graduates will ultimately choose non-STEM occupations. It is estimated, for example, that 26% of engineering graduates do not enter the engineering profession.
- 6.78** Sellafled Ltd have taken the approach a step further, and developed a Technical Specialist Trainee Scheme to address the shortfall of relevant skills in their sector.

¹²⁹ Royal Academy of Engineering, *Jobs and Growth: the importance of engineering skills to the UK economy*, 2012

Sellafield Ltd Technical Specialist Trainees (TST)

The Sellafield Ltd Technical Specialist Trainees (TST) is a development programme designed for young people looking to become qualified technical professionals. Sellafield Ltd developed the programme in partnership with GENII, a Cumbrian based training organisation, and together they designed a Foundation Degree in Nuclear Related Technology, to address some of the key technical and engineering skills shortages in the nuclear industry.

The scheme consists of a full time bridging programme based at GENII (three months), followed by part time study (day release for three years) and appropriate work-based assignments. The Foundation Degree provides the nuclear industry with an important tool for the recruitment and development of technical specialists for the future.

The trainees gain real work experience together with an accredited foundation degree without accruing any debt. Sellafield Ltd recruits approximately 12 technical trainees per year. The targeted recruitment and development of young local talent has resulted in excellent retention rates of 97%.

Recommendation 85: Higher Education courses should, wherever appropriate, be a collaboration between employers and universities. For shortage subjects for which there is strong employer demand, universities and employers should develop models where a commitment from firms of between a third and a half of a student's course fees will commit the student to working for that employer for a fixed number of years after graduation. This should be taken forward by the relevant Industry Councils.

Immigration and skills

6.79 The Government faces two pressures on immigration. On the one hand there is pressure from business for streamlined access to qualified foreign workers to address domestic skills shortages – particularly in science and engineering disciplines where shortfalls are projected to be ongoing. The education sector too needs a welcoming environment for foreign students because this is an important market in which the UK excels.

6.80 Our first responsibility, of course, should be to train the engineers – and other workers that we need – ourselves. However, even if there were an immediate increase in the number of students starting engineering degrees it would be at least a decade before they could begin to fill the full range of engineering vacancies in the economy. In the meantime, immigration is the only option.

- 6.81** The other pressure points us in a different direction. It is a pressure to reduce the overall numbers of immigrants and curtail low skilled immigration. Above all, there is pressure to identify, locate and eject the illegal migrants and over-stayers.
- 6.82** This government, like previous governments, is struggling to respond to both pressures. Businesses continue to see immigration controls as burdensome and bureaucratic. The fact that the annual quota for skilled immigration is currently undersubscribed by 35% despite complaints from business about skills shortages, is probably indicative of a system that business sees as difficult to navigate. At the same time we are not doing enough to tackle illegal migrants and over-stayers, and are struggling to tackle the backlog of refused residency applications from individuals who are already in the country. Some of these illegal migrants will be filling low skilled jobs that could and should be taken by British citizens and legal residents. The large numbers of migrants apparently living in unsuitable accommodation in London and elsewhere is of deep concern.
- 6.83** It goes almost without saying that the ideal solution is a well-managed immigration system that is open and welcoming to those who can address our skills gaps and add value to the economy, yet is unattractive to those who do not have and would not get permission to be here. This is easier said than done at a time of tough manpower constraints in the public sector.
- 6.84** Where there is a skills shortage in the UK, the Government is already committed to a system that allows businesses to bring in the best people from across the world to strengthen their workforce. That is right, and is a policy that needs to be informed by the independent Migration Advisory Committee and better-publicised.
- 6.85** I have three further suggestions. First, the Government should look at whether the sponsorship and application processes can be streamlined and made more business-friendly without making the system more vulnerable to abuse. Better regulation principles should be applied to ensure that the Government's policy aims are not frustrated by unnecessary bureaucracy.
- 6.86** Second, government should commit more resources to tackling illegal immigration and over-stayers, as well as the backlog of residency applications. The perception that this is not being prioritised by government has the effect of undermining confidence in immigration policy more generally.
- 6.87** Third, in line with the approach I recommend throughout this report, I believe there should be a coordinated government initiative, led by the Home Office, to ensure that all aspects of government policy work in unison to discourage illegal immigrants and limit access to resources and services to which they are not entitled.
- 6.88** It is only by tackling illegal immigration effectively that we can build the confidence and public assent to welcome the skilled workers that we actually need or the students who can contribute so much over time to our interests and well being.

Recommendation 86: The Home Office should undertake a targeted communication programme to improve business understanding of the skilled worker immigration rules to align perception and reality.

Recommendation 87: Government should review the regulations relating to immigration policy as part of the Red Tape Challenge process.

Recommendation 88: Government should accelerate the pace at which it is tackling illegal immigration, over-stayers and the backlog of residency applications. It should do this through a significant but temporary redeployment of public sector people and resource. The backlog should be tackled on a task and finish basis, with clear targets and milestones, so that the redeployment does not become permanent.

NO STONE UNTURNED in pursuit of
GROWTH

Chapter 7:

Making it happen

- 7.1** If there is an upside to the worst economic crisis of modern times it is the emergence of an audience for deep seated and radical proposals.
- 7.2** They distrust talk of isolated initiatives or quick wins. An ever more competitive world will only become more competitive not less. The structures and attitudes of yesterday did not work that well then and certainly will not cope with the new world order.
- 7.3** I can only present my suggestions. I have looked at our many successes and sought to build on them. Where they exist I advocate their extension.
- 7.4** My report does not single out a few headline making initiatives for those areas we need to improve. Instead I urge reforms that create a more effective partnership between government in London and the many different communities across the country that make us what we are. Central government must do less but do it better, share more of its power and show greater trust in local people and organisations.
- 7.5** The drivers of our economy – business, central government and local leadership – should be organised and structured for success. I have therefore re-assessed the way we, as a country, currently conduct business and re-evaluated each of our roles with the single overall aim of embedding a culture of wealth creation. As the saying goes we are all in it together.
- 7.6** To achieve this, I believe we need to ensure the following:
- > local communities empowered and incentivised to collaborate for growth
 - > a rejuvenated partnership between the public and private sectors involving both local and central government
 - > a dynamic, strategic central government with wealth creation at its heart, working more effectively in the national interest to support wealth creation and embracing a culture of both public and private sector decision making
 - > a private sector led business support infrastructure accessible everywhere
 - > a system for producing the skills that our economy needs now and in the future
 - > businesses, irrespective of size, sector or location which are engaged with their wider communities and ambitious to grow.
- 7.7** Central to my vision are enhanced roles for both LEPs and the chambers of commerce. I know critics will say that these bodies do not in all parts of the country currently have the capacity to deliver my vision. I have sat in the committees of government and heard those arguments many times. Indeed they are a central part of our problem. Because the scepticism is so deep about empowering local organisations, whenever faced with a problem the solution has been to take central control.

- 7.8** I am not interested in a debate about the present talent or energy of local organisations – although I would like to say that very many of those that I visited for this review were every bit as capable as those in the centre of government. But that is not the point. If some organisations are not up to the job the solution is to improve them, not to centralise further. No company with an underperforming subsidiary would move all its activities to head office.
- 7.9** It is important that local people are themselves satisfied that they have, in their areas, the quality of leadership needed for a real economic partnership with Whitehall. The LEPs and chambers are essential building blocks in our competitiveness agenda. Without such local empowerment we will not transform our national performance.
- 7.10** Implementing my blueprint will not be easy. It requires will and determination. It requires long term stability which can only be achieved with the maximum political consensus. There is nothing inherent in my vision which should appeal more to one party than another. The willingness to create wealth by working with public and private sectors and in partnership with local economies should be shared across the parties. There may be a proper debate about how the wealth is divided, but it is a sterile debate if the wealth is not created in the first place.
- 7.11** As with every plan it is the implementation that will be crucial. In the event that my report commends itself to government I set out below a possible timetable for implementation.

Central government	Timing
National Growth Council established, with a shadow committee of permanent secretaries and a secretariat	January 2013
Strengthened role for departmental Non-Executives in business planning and senior appointments	January 2013
First iteration of departmental growth commitments	March 2013
Local Growth Teams established across England	April 2013
Ministers and permanent secretaries identified to champion LEPs	April 2013
Each department to publish a comprehensive organogram showing the deployment of its staff	April 2013
Removal of barriers to departments recruiting externally for key skills	April 2013
New Whitehall management information system introduced	April 2013
National Growth Strategy published	May 2013
Formal sector partnerships established with lead departments, and lead trade associations identified	July 2013
Sector strategies agreed between business and government	April 2014

Central government	Timing
Mechanism established to facilitate secondments between public and private sectors	April 2014
Civil Service Learning to adapt portfolio to maximise joint training for public and private sector at all levels	April 2014
Government decides outcome of LEP bids and allocates funds for five year period	June 2014

The new partnership	Timing
Government confirms arrangements for LEPs to review their boundaries and to develop local growth strategies	January 2013
LEPs devise strategic plans and bids to access funding in consultation with stakeholders	January 2013 – January 2014
LEPs confirm boundaries or propose changes	By March 2013
Government confirms indicative budget for single pot	April 2013
National Growth Strategy published	May 2013
Government endorses revised LEP boundaries	By June 2013
LEPs submit bids to central government	February 2014
Government announces outcome of initial round of bidding and the allocation of funding	July 2014
LEPs begin to access funds	April 2015

7.12 Any strategy for implementation will be more effective if the process involves people, first, from outside government who have experience of the private sector and, second, represent the LEPs and local government upon whom the success of the new partnerships depend.

Recommendation 89: An experienced implementation team should be set up in the centre of government, including secondees from the private sector, LEPs and local authorities.

7.13 Finally if I could ask one thing of government it is that it sees the publication of this report as the opportunity for a debate on the issues raised. I would be naive if I were not already aware of those who are resistant to some or all of what I suggest. They are right to express their concerns. But those concerns should be weighed against the back drop of the scale of our international competitive challenge. Continuing as now is not an acceptable option. The world will not stand still – and nor must we.

Annex A:

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Annex B:

Summary of recommendations

Localism – building on our strengths

1. Central government should identify the budgets administered by different departments which support growth. These should be brought together into a single funding pot for local areas, without internal ring fences.
2. Local partnerships should bid for funds from central government on a competitive basis. Bids should be for a minimum of five years starting from 2015/16.
3. Government should streamline its management of EU Common Strategic Framework funds in England, strip out the bureaucracy of multiple programmes and align local allocations from the four funds with the single funding pot.
4. Taking full account of the Government's national growth strategy, all LEPs, in collaboration with local stakeholders, should lead the development of a long term strategy and business plan for their area that will be used to bid for economic growth funds from central government.
5. The Government should allocate LEPS up to £250,000 of new public funding, resourced through departmental efficiency savings and underspends, in each of years 2013/14 and 2014/15 specifically to devise their local economic strategies, and create the foundations for their implementation.
6. The Government should invite LEPs to review their boundaries within a three month period to ensure they have a good match with their functional economic market area and that they do not overlap.
7. In light of the new role and vision for LEPs, each LEP should ensure that their board has the necessary skills and expertise to deliver their expanded functions and pay particular attention to the representation of employees from both private and public sector.

8. At the earliest opportunity civil servants based across the country should be brigaded into Local Growth Teams, structured around clusters of LEPs, primarily tasked with joining up government and local partners in the areas of their responsibilities to facilitate, identify and realise economic opportunities.
9. Ministers and permanent secretaries should be associated with individual LEPs, not to advocate individual plans but to add an understanding of place to the existing culture of function.
10. Local authorities should have a new overarching legal duty to have regard to economic development in the exercise of all their activities and functions. Where local authorities share a functional economic market area they should be required to collaborate on economic development.
11. All two-tier English local authorities outside London should pursue a path towards unitary status. The Government should encourage this and work with authorities to clarify the process and enable it to happen.
12. Proposals for formal collaboration between local authorities that reinforce the standing of the LEP and enhance the partnership with the private sector across a functional economic market area, should be encouraged and prioritised for government approval. All proposals to move to unitary or combined authority models should be scrutinised by the Prime Minister's Growth Council.
13. The Government should remove all legislative barriers that are preventing local authorities from collaborating within functional economic market areas, including moving to a unitary status.
14. Local authority council members should be elected using the same electoral cycle across England where the whole council is elected at the same time every four years.
15. Legislation should be passed to enable combined local authorities, and other combinations of authorities, that wish to elect a conurbation mayor to do so.

Whitehall – a confident, strategic centre of government

16. The Government should produce an overarching and long term National Growth Strategy and its vision for wealth creation, with concrete commitments against which it can be held to account.
17. A new National Growth Council should be established, chaired by the Prime Minister and with a strong, cross-government focus on driving growth and wealth creation.
18. Operational responsibility for implementation of the National Growth Strategy should rest with a designated minister, supported by a secretariat.

19. Government should establish a shadow Growth Council of permanent secretaries and Non-Executives chaired by the designated minister to drive implementation of the Growth Strategy across all departments.
20. Departments should include a growth commitment in their annual business plans setting out their contribution to the Growth Strategy over the previous year and planned action for the coming year. This should explicitly include how departments will use the economic levers available to them to support growth over the long term.
21. The role of Non-Executives in the development of growth commitments and departmental business plans should be strengthened and formalised. Non-Executives should have access to the Growth Council secretariat to support their enhanced role.
22. Departments should work with the public bodies they sponsor to ensure they explicitly consider their potential for wealth creation when developing business plans.
23. Government must continue to look at opportunities for devolving or transferring the functions of public bodies to the local level or to the private sector.
24. A Whitehall management information system must be introduced and should encompass management and financial data as set out in Annex F.
25. The Cabinet Office should work with departments to remove restrictions on departments recruiting externally for key skills and professionals – including disapplying general pay ceilings, recruitment freezes and redeployment pool policies. In making recruitment decisions, departments should focus on controlling their total salary costs. Where a recruitment breaks a pay ceiling, departmental Non-Executives should give their approval to the process and the appointment.
26. Departmental Non-Executives should be able to make recommendations on the appointment of permanent secretaries.
27. Barriers to secondments between the public and private sectors should be removed and secondment programmes in government departments should be reinvigorated.
28. Civil Service Learning should develop courses aimed at encouraging public and private sector people at all levels to train together.
29. Civil Service Learning should be recreated as a commercial body to train civil servants to perform more strategic roles and develop expert policy knowledge, and to market its services overseas.
30. Government departments should offer all major sectors of the economy the opportunity to form a relationship with government.
31. The Department and the sector should agree an appropriate level of interaction which is endorsed by the Growth Council. Each relationship should be set out in departmental growth commitments.

- 32. Lead departments should coordinate the Government's interaction with each sector, ensuring there is a constructive dialogue with mutual understanding and shared ownership of outcomes.
- 33. An Industry Council should be established for each formal partnership between government and a sector.
- 34. Government departments and industry sectors should jointly nominate lead trade associations to represent sectors in their dialogue with government and encourage the private sector to bring about a major rationalisation of trade associations to enhance the quality of the debate.
- 35. Government should increase the number of companies managed through the Strategic Relationship Management model and this should be used by all government departments.

Government and growth – catalyst, enabler, partner

- 36. Every government department should recruit a Chief Procurement Officer at competitive market rates, reporting direct to the permanent secretary, to lead the procurement and delivery of major projects and improve the capabilities of their procurement cadre. The department's Non-Executives should approve the selection process and appointments.
- 37. The Cabinet Office should place a general duty on all public bodies, setting out the procurement standards to which they should adhere, by providing a pan-government procurement strategy, legislating if necessary.
- 38. The Government should go further in its plans to build strategic relationships with industry, ensuring that the long term impact on technological advantage and the UK industrial base are taken into account in the procurement of specialist technologies.
- 39. The Government should continue to commit to the long term stability of the core funding of science and research, at a level which keeps pace with our international competitors.
- 40. UKTI should work with the Technology Strategy Board and the Research Councils to strengthen the marketing of the UK as an inward investment destination on the back on our world-renowned research excellence.
- 41. The Department for Business, Innovation and Skills and the Technology Strategy Board must set out a clear statement explaining how they and other government agencies will work with LEPs and the devolved administrations to better connect national strategy with local initiative.
- 42. All government departments, working through the Chief Scientific Advisers Committee, should consult with the Technology Strategy Board and Research Councils UK on the development of their growth commitments.

43. Rather than setting up duplicate teams across government, a single source of expertise for innovative procurement should be established that builds on existing work and successful mechanisms. This resource should help to aggregate demand and coordinate activity around shared innovation challenges, provide expertise, coordination and guidance, and scale up and develop innovative procurement initiatives.
44. The British Standards Institution, Technology Strategy Board and Research Councils UK should work together to ensure that new standards are set earlier in the development of new technologies in the UK.
45. The Government should survey the practices and procedures of all regulators involved in conjunction with the sectors affected with a view to simplifying procedures and avoiding unnecessary duplication between agencies.
46. Government should involve the private sector in drafting regulations so it is a collaborative process. It should invite trade associations, through the lead associations for their sectors, to submit precise redrafting of existing regulations prior to wider consultation on any changes.
47. Through its review of both the Principles of Economic Regulation and the Compliance Code for non-economic regulators, the Government should impose an obligation on regulators to take proper account of the economic consequences of their actions.
48. In preparing for any review process, regulators should invite the lead sectoral trade association (or a national body in the case of horizontal regulators) to analyse and publish evidence on the impact of the regulator's activities – both what it does and how it does it – on the businesses affected. This published evidence would then be available for analysis and comment by other interested parties.
49. Regulators should set out their service standards and cost recovery policies clearly, showing how much they will charge under what circumstances.
50. Regulators should publish policy statements showing how they will ensure that their decisions are both internally consistent across their geographic area, and consistent with those of any other bodies which regulate the same businesses.
51. All regulators should adopt systems of earned recognition and meet the cost of inspections carried out at the discretion of the regulator within any recognition period.
52. All non-economic regulators should publish policies showing how their customers can ask, without prejudice, for an independent second opinion on a regulatory decision or requirement.

- 53.** The Government must continue to promote the British interest in Europe and all secretaries of state with EU business affecting their department should make bi-annual trips to Brussels to influence decision making throughout the EU policy making process. All departmental ministers with EU business should consider every proactive step possible to put Britain on the front foot at the negotiating table.
- 54.** Government departments should develop greater capacity to identify forthcoming EU regulations well in advance.
- 55.** The Planning Inspectorate should be given powers to investigate planning decisions proactively. The Government should also consider on a rolling basis all the possible options to inject urgency and purpose into the planning system.
- 56.** The Government should consider the effectiveness of Local Development Orders and extend their use after consultation with affected parties to establish best practice.
- 57.** The Government should consider using Special Development Orders to speed up specific planning decisions of strategic significance.
- 58.** The Government Property Unit should work with local authorities to identify and publish details of all surplus and derelict public land on the ePIMS database so that LEPs and local authorities can collaborate to bring this land back into reuse in support of the local economic strategy.
- 59.** The Government should set up a new Development Corporation under an independent chairman from the private sector, comprised of representatives of central government, the Mayor of London, London boroughs, Kent and Essex councils and with a majority of members from the private sector and related disciplines. It should not exceed 20 members. Once created the Corporation should be given the powers it needs to drive its vision for future growth. It should be able to bid for its funds from the single pot.
- 60.** The Government should accept the need to clarify urgently its preferred solution to the problem of airport capacity in the South East and indicate that preference whilst making its implementation conditional on the outcome of the next election.
- 61.** The Government needs to set out a definitive and unambiguous energy policy, including the supporting financial regime, to give the sector the certainty to invest.
- 62.** The Government should initiate discussions through the Bank of England and, in cooperation with the appropriate regulators, seek one or more solutions to enable UK pension funds to invest in UK infrastructure assets. The Government should ensure that best practice applies to both public and private sector pension fund investments.

Private sector – broadening the capacity for excellence

- 63.** The chambers of commerce could benefit from an enhanced legal status to support their role as coordinating hubs for business support and engagement at local level. The Government should consider legislating to give chambers basic statutory functions, whilst guaranteeing their continuing independence from government. It should provide for compensation if government opts out of these arrangements.
- 64.** Government and the private sector should collaborate to create a strong and stable, locally-based, private sector business support infrastructure. This should be centred on an enhanced role for chambers of commerce. At the minimum, government should pursue option 2 and take all appropriate steps to secure its implementation.
- 65.** Local authorities should publish the list of all businesses paying non-domestic rates so that chambers and other business representative bodies can identify businesses in their area more reliably, and seek to draw them into the local businesses support initiatives. There should be exceptions for businesses where the identification of business premises could give rise to security concerns.
- 66.** An updated Code of Practice for Trade Associations should be developed. It should be given teeth by making compliance with the Code a condition for membership of the Trade Association Forum.
- 67.** The Trade Association Forum should press ahead with the development of a competency framework for individuals to drive up professionalism within trade associations.
- 68.** The Trade Association Forum should develop an enhanced directory of associations which is easily navigated through keyword searches.
- 69.** In developing their economic plans, LEPs and chambers should consider ways in which leadership and management capabilities in local businesses can be raised making full use of local networks, local training providers and businesses themselves. Plans could, for example, incorporate commitments from large corporates and leading mid-size businesses to help raise leadership and management capacities in their supply chains.
- 70.** The development of leadership and management skills should be integrated, where appropriate, into the education and skills system at every level, from schools through to higher education and vocational skills training. We need to see individuals having opportunities to develop their leadership and management capabilities earlier on in their working lives, alongside the development of technical or academic competencies.
- 71.** As part of their growth commitments, departments should set out plans for sector-based supply chain programmes, learning from the experiences of the Advanced Manufacturing Supply Chain Initiative.

- 72.** Government should ensure the availability of long term patient loan capital to growing businesses which do not want to dilute their equity. It should give serious consideration to tasking the new Business Bank to provide this either by itself or in partnership with the Business Growth Fund.
- 73.** The Government should take a greater interest in foreign acquisitions from the perspective of the UK's industrial strategy priorities, using an enhanced sector knowledge and expertise. Government should do far more to engage with potential foreign investors in our core sectors to secure commitments to developing the UK research, skills and supply base, and in exceptional cases to discourage unwanted investments. We should underpin this by signalling a greater readiness to use existing powers in the Enterprise Act 2002 to allow ministers to consider takeovers and mergers to ensure our long term industrial capabilities are given proper consideration.

Education and skills – the foundation for growth and prosperity

- 74.** All failing schools should be subject to the intervention process forthwith. There should be a clear timetable within which an improvement strategy for each school is agreed, with the education authorities using their powers to intervene if the head teacher and governors fail to act. If local authorities delay, central government should intervene.
- 75.** The regional directors being appointed to lead Ofsted's new regional structure should be given formal powers to act swiftly where they identify problems in local schools.
- 76.** Business engagement should be incorporated far deeper into the school curriculum in order to develop young people's understanding of business, increase their employability, and further their understanding of career and future training options and where they might lead. LEPs should consider how they engage with local schools and work with chambers to facilitate this.
- 77.** The bureaucracy and paper work around work experience and work placements must be streamlined. DfE must be clear about what is absolutely necessary. Government must then ensure the removal of all regulations and requirements that place unnecessary burdens on employers, schools and colleges.
- 78.** All boards of governors in secondary schools should include two influential local employers, at least one of whom should have good connections with the wider business community. This could be coordinated by the local chambers of commerce.
- 79.** Local authorities should publish the Destination Measures for all secondary schools in their areas alongside academic attainment so that parents can make better informed choices, and to incentivise schools to give a higher priority to developing the employability of their leavers.

80. The existing budget lines for adult careers advice should be included in the single funding pot. Each LEP, as part of its local economic plan, should consider how careers advice is best provided in its area to meet the needs of both the adult population and the requirement under the Education Act 2011 for careers advice in schools.
81. The budget for vocational training for learners aged 19 and over, and all funding currently set aside for apprenticeships for those aged 16 and over, should be devolved to local areas through the single funding pot described in Chapter 2. This therefore calls into question the continuation of the Skills Funding Agency. Each LEP should incorporate skills needs within their local economic plans driven by the needs of local employers and the practical experience of FE colleges.
82. All FE learning providers must consult and agree their provision with LEPs to ensure that the courses they offer to 16-18 year olds reflect local labour requirements. In addition, any vocational courses delivered by FE providers to learners of any age must conform to the defined national standards set by employers and industry.
83. Action to address NEETs is best taken at the local level. Resources to tackle the problem should therefore be available from the single pot. Youth unemployment will not be a problem or priority for action in every area, but where it is, LEPs working with local authorities, employers and other local partners should develop proposals for reducing NEET numbers as part of their local economic plans.
84. Industry Councils should work with the higher education sector to ensure that courses are relevant, incorporate placements in industry, and match the skills for which there is demand. Government needs to consider incentives to encourage and develop this further.
85. Higher Education courses should, where appropriate, be a collaboration between employers and universities. For shortage subjects for which there is strong employer demand, universities and employers should develop models where a commitment from firms of between a third and a half of a student's course fees will commit the student to working for that employer for a fixed number of years after graduation. This should be taken forward by the relevant Industry Councils.
86. The Home Office should undertake a targeted communication programme to improve business understanding of the skilled worker immigration rules to align perception and reality.
87. Government should review the regulations relating to immigration policy as part of the Red Tape Challenge process.
88. Government should accelerate the pace at which it is tackling illegal immigration, over-stayers and the backlog of residency applications. It should do this through a significant but temporary redeployment of public sector people and resource. The backlog should be tackled on a task and finish basis, with clear targets and milestones, so that the redeployment does not become permanent.

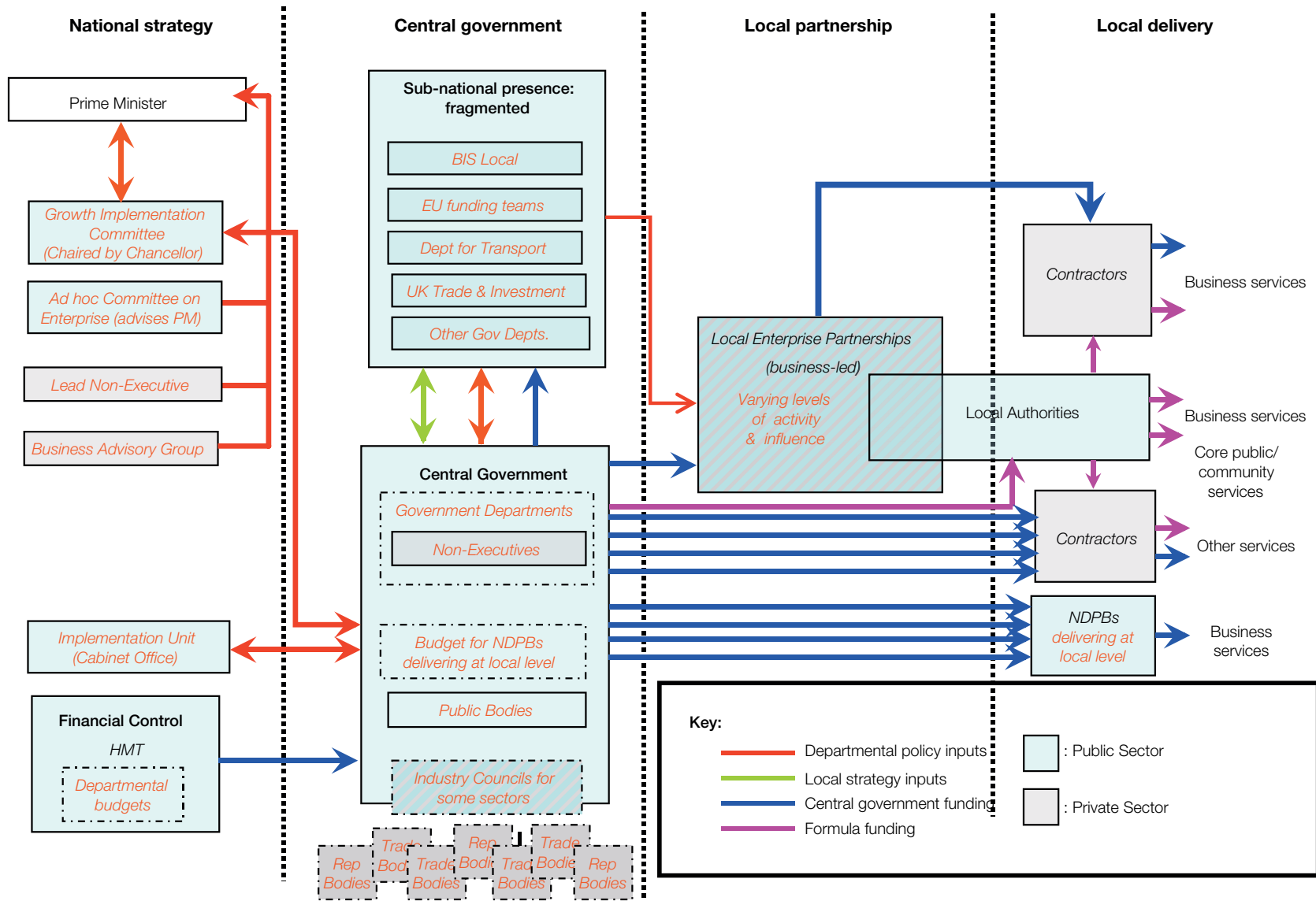
Making it happen

- 89.** An experienced implementation team should be set up in the centre of government, including secondees from the private sector, LEPs and local authorities.

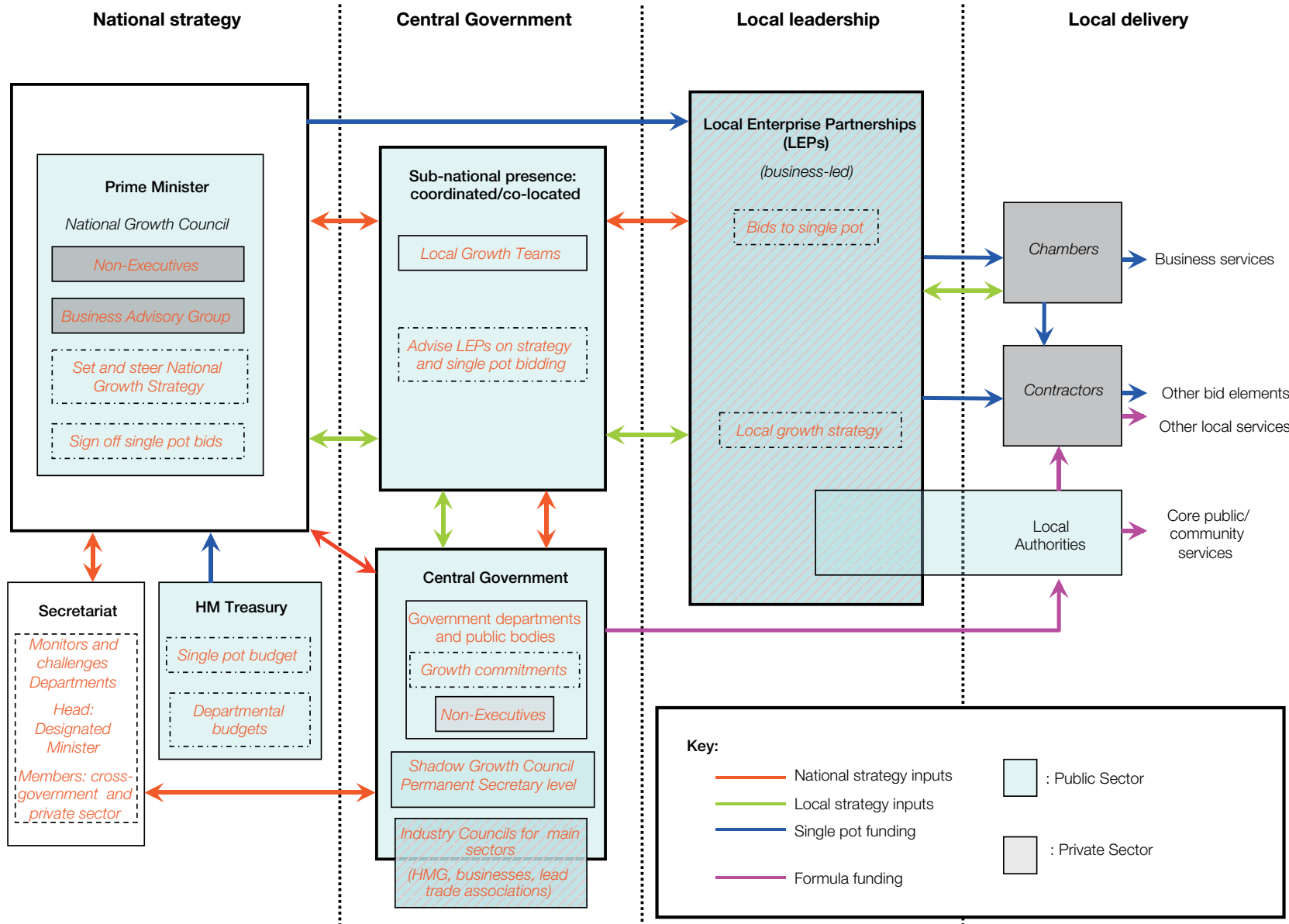
Annex C:

How the system fits together

Current structure for delivering growth



Proposed new structure for delivering growth



Annex D:

Single funding pot

	Current funding stream ¹²⁰	Department	4 year period (£ million)
Skills	Adult Skills Budget (includes 19+ apprenticeships)	BIS	10,708
	Offender Learning and Skills Service	BIS	528
	Community Learning	BIS	848
	Learner Support	BIS	658
	Information Advice and Guidance	BIS	338
	Skills Infrastructure	BIS	251
	Capital Grants	BIS	1,078
	Apprenticeships (to 18 year olds)	DfE	3,036
	Skills total		17,435
Local infrastructure	Local Authority Capital		8,000
	Broadband delivery UK – roll out in rural areas	DCMS	530
	Broadband super connected cities	DCMS	150
	Broadband mobile infrastructure	DCMS	150
	Rail Industry R&D Funding	DfT	36
	Accelerating Innovation in Rail	DfT	10
	Local transport projects	DfT	1,700
	Growing Places Fund	CLG	730
	Tax Increment Finance Schemes	HMT	150
	Green Deal	DECC	200
	DECC Innovation Programme	DECC	200
	Waste PFI credits	DEFRA	338
	Flood defences	DEFRA	2,628
	Local infrastructure total		14,821

¹²⁰ All numbers presented to nearest £ million. Totals do not equal the sum of the rows due to rounding.

	Current funding stream	Department	4 year period (£ million)
Employment support	Work Programme	DWP	2,542
	Remploy Work Choice	DWP	884
	Specialist and Flexible Programmes	DWP	1,040
	Youth Contract	DWP	1,000
	Employment support total		5,466
Housing	New Affordable Housing	HCA	4,500
	Decent Homes	HCA	2,100
	FirstBuy	HCA	200
	Housing total		6,800
Business support services	Regional Growth Fund	CLG	2,400
	National Call Centre	BIS	13
	Growth Accelerator	BIS	140
	Leadership and Management Advice	BIS	54
	Business in You campaign	BIS	1
	Designing Demand	BIS	5
	Rural Growth Networks	DEFRA	15
	Manufacturing Advisory Service	BIS	15
	Creative England	DCMS	1
	Waste and Resources Action Programme	DEFRA	130
	Passport to Export	UKTI	8
	Gateway to Global Growth	UKTI	2
	International Trade Advice	UKTI	78
	High Value Opportunities Programme	UKTI	12
	Export Marketing Research Scheme	UKTI	4
	Tradeshaw Access Programme	UKTI	27
	Missions (Inbound and Outbound)	UKTI	5
	Export Communications Review	UKTI	1
	Sector Events	UKTI	30
	Business support total		2,939

	Current funding stream	Department	4 year period (£ million)
Innovation and Commercialisation	Technology Strategy Board thematic funding	BIS	758
	Catapults	BIS	270
	Small Business Research Initiative	BIS	34
	Knowledge Transfer Networks	BIS	62
	Knowledge Transfer Partnerships	BIS	94
	Smart	BIS	170
	Eurostars	BIS	27
	Launchpads	BIS	24
	Health Innovation Challenge Fund	DH	80
	i4i product development awards	DH	52
	Marine Energy Array Demonstrator	DECC	20
	BSI Targeted Funding	BIS	20
	Innovation and Commercialisation Total		
	Total		49,073

Annex E:

Illustrative single funding pot bidding framework

I am the first to recognise that the document that follows appears bureaucratic. It is. Any partnership involves accountability and properly so. This system however is only a much simplified version of what already exists. But instead of the myriads of individual control systems designed to tick functional accountability of the present arrangements, this method draws the process into one place-based system.

This illustrative framework sets out the requirements LEPs would need to address to secure funds from a single competitive pot. In drawing up such a framework, the Government would need to consult LEPs, local authorities and the business community.

The requirements include:

1. Contribution to national strategic priorities as set out in the Government National Growth Strategy

The Government will set out the strategic national priorities for UK competitiveness and growth. This will follow the coordination of departmental growth commitments as well as setting its long term policy vision. It will set out the aspects of the strategy that need to be led by other economic partners as well as central government departments. In particular it will describe the national priorities which the Government will wish to ensure are met, on aggregate, by the LEP strategies.

This plan will describe the overall national vision for economic growth: the UK's aggregate strengths, weaknesses, opportunities and threats, and set goals for future competitiveness (such as its existing export targets). Local leaders will develop their own economic strategies within the context of this national vision. The plan will include priorities that are of national significance but for which central government wishes a greater partnership with local communities. Examples of these include geographically specific investments or services that will be provided at the local level.

These priorities are likely to cover a wide range of policies including innovation, education and skills and housing and the interrelationship of these policies to wider social objectives.

Bids will be judged to a significant extent on their contribution to national strategic priorities, including the relative economic return for the funding provided. LEPs should identify the local actions that best enable them to meet these objectives. They will be assisted by Local Growth Teams who will also facilitate cooperation with NDPBs, such as the Technology Strategy Board, Homes and Communities Agency and sector skills councils.

This devolved process does not absolve the Government of its statutory responsibilities. LEPs must ensure that their bids meet these conditions. For example, there is currently a statutory entitlement to 'Skills for Life' – basic literacy, numeracy and English Language for Speakers of Other Languages – for all those over 16 years that have left compulsory full time education and do not have up to date qualifications. The Government must of course keep under review these type of obligations to ensure that they continue to meet policy objectives.

2. Engagement with local public bodies, businesses and residents

Bids must demonstrate a thorough and comprehensive consultation process as part of all submissions. They should also make clear how the LEPs will continue to engage with these parties through the lifetime of the plan to be accountable to their local communities.

3. LEP corporate governance

LEPs will need to demonstrate robust corporate governance, in particular fiscal probity and managing conflicts of interest.

4. Delivery

a. Relationship with chambers

LEP bids must nominate an accredited chamber of commerce to act as partner, responsible for the coordination of all business service delivery as set out in the LEP plan. The named chamber could, if it chooses, work with a consortium of other chambers to deliver its functions.

Should an accredited chamber not exist within the LEP area, that LEP should nominate an accredited chamber of commerce of their choice to fulfil the above function.

b. Relationship with other providers

The bids will also need to set out how the LEP will work with local and national partners to deliver all its other services.

5. Data collection and submission, monitoring and evaluation

LEPs' bids must be in compliance with a Common Impact Evaluation Framework. This framework will be developed in consultation with LEPs and other partners. The aim of this framework is to enable the eventual assessment of the outcomes achieved by LEPs (both local outcomes and the contribution to national outcomes). This data will enhance the local evidence base, assisting LEPs in developing their forward looking economic strategies based on a better understanding of which interventions work best, how they work and under what circumstances. A common methodology and data system will also assist government in determining the potential impact of individual bids. Additionally, it will facilitate the spread of innovative investments, processes and best practices between LEPs.

Evaluation should be based on the following principles:

- > formal planning and preparation for evaluation that takes account of national strategic priorities as well as local objectives
- > commitment of corporate resources, budget and support to evaluate activity
- > effective and cost-effective management of evaluation
- > transparency, independence and inclusiveness in the conduct of evaluations; and dissemination of and learning from the results of evaluation to inform future activity.

6. Estimated investment leverage

Bids will be expected to demonstrate a significant amount of match-funding committed to development plans from local and national partners – including private sector funding or co-funding, lottery, EU structural funds and local authority capital receipts. This will be a central element in evaluation of LEP bids.

Annex F:

Key elements of a government management information system

What the system should do

A good management information system should bring together operational and financial information to measure both inputs (resource and activity) and outputs (performance and impacts). It should make clear who is in charge and ensure effective accountability by linking budgets and performance to the individuals responsible for them.

The information should allow permanent secretaries and ministers to see how resource is being used across their department and have meaningful discussion of performance against plans. It should also support discussions between officials and ministers on the impact and value for money of existing activity and resourcing of future priorities. It will help identify where extra resource is needed, where savings can be made, including shutting down activity, and areas that may be suitable for transferring to a different delivery model.

What the system should provide

The system should present the purpose and main areas of responsibility for each team (generally branch level – in most cases these will be senior civil service, deputy director-led teams) and an organisation chart showing the structure of each team, with the grade and role of each team member.

The key output of the system should be data showing progress against the overall expected outcomes and specific performance measures (see example overleaf). This data should include:

(i) the financial expenditure and man days devoted to each outcome and related activity; and
(ii) a report of the impact of each activity. The information should set out both plans and outturns, facilitating interrogation of any variance between them. It should show at least one previous period's outturn, allowing comparison over time.

What the system needs

There must be a single system with common reporting standards that make sense to the centre and departments. Departments must be able to accurately measure the number of man days devoted to each activity.

There should be a strong central team that provides:

- > **Leadership**: a clear point of responsibility to ensure departments deliver robust management and financial information.
- > **Central co-ordination**: central oversight to support and challenge departments.
- > **Analytical function**: an independent analytical view to ensure a well informed debate on information coming out of the system.

Proposed output from enhanced management information system

Team Telecommunications policy

Purpose The team covers all of the communications industry. The objective is to enhance the competitiveness of the industry, its service to customers and the competitiveness of its supply chain.

Team leader John Smith

Performance against functions

Function	Staffing (man years)				Budget (£000s)				Performance	Performance			
	Previous year Outturn	Current year			Previous year Outturn	Current year				Previous year Outturn	Current year		
		Plan	Outturn	Variance		Plan	Outturn	Variance			Plan	Outturn	Variance
Licencing: Issuing new licences to operators	9.3	11.7	9.6	-2.1	1715	1615	1600	-15	Licences issues within 3 months	45%	80%	70%	-10%
Sponsorship: establishing dialogue with industries	3.5	3.5	5.1	1.6	450	400	410	10	Decisions overturned on appeal	25%	10%	5%	-5%
									Dialogue meetings with industry (meetings per year)	23	30	32	2
Competitiveness: agree skills strategy		6.5	5.5	1.0	500	520	520	0	Feedback from industry CEOs (% positive)	35%	75%	90%	15%
									Strategy signed off by sector group		45%	50%	5%
Competitiveness: supply chain initiative		3.0	2.5	0.5		700	750	50	Feedback from launch event		20%	20%	0
									Analytical paper completed		10%	20%	10%
									Consultation phase		50%	50%	0
									Deliver comms plan		40%	40%	0
TOTAL	12.8	24.7	22.7	1.5	2665	3235	3280	45					

Information in this table is for illustrative purposes only

Team Telecommunications policy

Purpose The team covers all of the communications industry. The objective is to enhance the competitiveness of the industry, its service to customers and the competitiveness of its supply chain.

Team leader John Smith

Performance against functions

Function	Staffing (man years)				Budget (£000s)				Performance	Previous year Outturn	Current year		
	Previous year Outturn	Current year			Previous year Outturn	Current year					Plan	Outturn	Variance
		Plan	Outturn	Variance		Plan	Outturn	Variance					
Service: Improving coverage and service quality across the UK	10	8	8	0	10000	900	810	90	Coverage mapping exercise				
Boradband: Delivery of superfast broadband access	30	22	25	3	15000	20000	22000	2000	Signal quality testing	25%	20%	30%	10%
									Black hole assessment	10%	10%	12%	2%
									Ofcom Liaison Committee		5%	7%	2%
EU regulatory landscape	10	8	8	0	8000	7400	7800	400	Local authority monitor	10%	15%	10%	-5%
									Rural coverage	10%	20%	20%	0%
									EU Spectrum Expert Group	5%	5%	3%	-2%
									New EU standards directive	5%	10%	12%	2%
									Telecoms Ministerial Conference		5%	5%	0%
TOTAL	50	38	41	3	33000	28300	30610	2490					

Information in this table is for illustrative purposes only

Annex G:

Glossary

AHK	German Chamber of Commerce overseas
BCC	British Chambers of Commerce
BERD	Business Enterprise R&D
BGF	Business Growth Fund
BIS	Department for Business, Innovation and Skills
BITC	Business In The Community
BRICS	Brazil, Russia, India, China and South Africa
BSI	British Standards Institution
CBI	Confederation of British Industry
CCTE	Chambers of Commerce Training and Enterprise
CEO	Chief Executive Officer
CIFIUS	Committee on Foreign Investment in the US
CLG	Department for Communities and Local Government
COSLA	Convention of Scottish Local Authorities
CSF	Common Strategic Fund
DCMS	Department for Culture, Media and Sport
DECC	Department of Energy and Climate Change
DEFRA	Department for Environment, Food and Rural Affairs
DfE	Department for Education
DfT	Department for Transport
DH	Department of Health
DIHK	Umbrella organisation for the German Chambers of Commerce and Industry
DIN	Deutsches Institut für Normung, the German Institute for Standardisation
DTI	Department of Trade and Industry (former BIS)
EAFRD	European Agricultural Fund for Rural Development

EEF	Engineering Employers Federation
EFA	Education Funding Agency
EMFF	European Marine and Fisheries Fund
ePIMS	Electronic Property Information Mapping Service
ERDF	European Regional Development Fund
ESF	European Social Fund
EU	European Union
FDI	Foreign direct investment
FE	Further Education
FEMA	Functional Economic Market Area
FPB	Forum for Private Business
FSB	Federation of Small Businesses
GCSE	General Certificate of Secondary Education
GDP	Gross Domestic Product
GERD	Gross Expenditure on R&D
GLA	Greater London Authority
GOVERD	Government expenditure on R&D
GSK	GlaxoSmithKline
GVA	Gross Value Added
HBOS	Halifax and Bank of Scotland Group
HE	Higher Education
HEFCE	Higher Education Funding Council for England
HEI	Higher Education Institutions
HERD	Higher Education expenditure on R&D
HKPC	Hong Kong Productivity Council
HMT	Her Majesty's Treasury
HO	Home Office
HS1	High Speed One
HS2	High Speed Two
IAC	International Automotive Components
ICFC	Industrial and Commercial Finance Corporation
IEB	Interim Executive Board
IHK	German Local Chambers of Commerce and Industry

IMF	International Monetary Fund
IoD	Institute of Directors
IPO	Initial Public Offering
IPR	Intellectual Property Rights
IT	Information Technology
JLR	Jaguar Land Rover
KfW	Kreditanstalt für Wiederaufbau (German government-owned development bank)
KPMG	Klynveld, Peat, Main and Goerdeler (Accounting Firm)
LA	Local Authority
LDDC	London Docklands Development Corporation
LDO	Local Development Order
LEP	Local Enterprise Partnership
LGC	The Laboratory of the Government Chemist
LOCOG	London Organising Committee for the Olympic Games
MA	Managing Authority
MI	Management Information
MINIS	Management Information System for Ministers
MoD	Ministry of Defence
MPA	Major Projects Authority
MRSA	Methicillin-Resistant Staphylococcus Aureus
NASA	North American Space Agency
NDPB	Non Departmental Public Body
NECC	North East Chamber of Commerce
NEET	Not in Education, Employment or Training
NESTA	National Endowment for Science, Technology and the Arts
NHS	National Health Service
ODA	Olympic Delivery Authority
OECD	Organisation for Economic Co-operation and Development
Ofsted	Office for Standards in Education
OFT	The Office of Fair Trading
ONS	Office of National Statistics
PAYE	Pay-as-you-earn tax
PFI	Private Finance Initiative

Pisa	Programme for International Student Assessment
PNFC	Public Non Financial Corporations
PPO	Prolific and Priority Offender scheme
R&D	Research and Development
RDA	Regional Development Agency
RGF	Regional Growth Fund
SBA	Small Business Administration (US)
SBIR	Small Business Innovation Research (US)
SBRI	Small Business Research Initiative
SDO	Special Development Order
SFA	Skills Funding Agency
SME	Small and Medium Enterprise
SMMT	Society of Motor Manufacturers and Traders
SRM	Strategic Relationship Management
STEM	Science, Technology, Engineering and Mathematics
TAF	Trade Association Forum
TECs	Training and Enterprise Councils
TSB	Technology Strategy Board
TST	Technical Specialist Trainees
TUC	Trades Union Congress
UDC	Urban Development Corporation
UKCES	United Kingdom Commission for Employment and Skills
UKTI	UK Trade & Investment
UNCTAD	United Nations Conference on Trade and Development
UTC	University Technical College
VAT	Value Added Tax
VET	Vocational, Education and Training
WEF	World Economic Forum
WTO	World Trade Organisation

‘What Manchester thinks today, the world will think tomorrow.’

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