House of Commons
Business, Energy and Industrial Strategy Committee

Industrial Strategy: First Review

Second Report of Session 2016–17

Report, together with formal minutes relating to the report

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**Business, Energy and Industrial Strategy Committee**

The Business, Energy and Industrial Strategy Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of the Department for Business, Energy and Industrial Strategy. The Committee’s name was changed, from the Business, Innovation and Skills Committee, on 17 October 2016.

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The current staff of the Committee are Chris Shaw (Clerk), Michael Everett (Second Clerk), Josephine Willows (Senior Committee Specialist), Ian Cruse (Committee Specialist), Becky Mawhood (Committee Specialist), James McQuade (Senior Committee Assistant), Jonathan Olivier Wright, (Committee Assistant) and Gary Calder (Media Officer). Martin Adams was Second Clerk of the Committee during this inquiry.

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List of Reports from the Business, Energy and Industrial Strategy Committee during the current Parliament
Summary

The Government’s re-found commitment to industrial strategy provides a significant opportunity to set a clear vision for what an “economy that works for everyone” should look like in practice, and put the UK on a path to reach it. We strongly support the Prime Minister’s aspiration of a stronger, fairer Britain “where wealth and opportunity are spread across every community.”

The Prime Minister’s rhetoric marks a significant shift away from that of previous Governments; consciously or unconsciously, it implies that the Government is willing to exchange some element of headline economic growth for more evenly distributed and resilient growth. At a time when Government is already having problems in balancing the books, any decision to slow the rate of short-term economic growth for other objectives (with a longer-term return) will make that task more difficult. Furthermore, success will only be achieved if policies are of a scale to match the Government’s ambition and clearly drive forward economic rebalancing.

But while the Government’s rhetoric marks a step change, and the creation of a new Department for Business, Energy and Industrial Strategy has significantly raised expectations, the Government’s approach appears to be evolutionary and reflects a continuation of policy approaches introduced from May 2015—a focus on horizontal policies, regional devolution, and sectoral “deals”. As it stands, there is a real risk that certain proposals benefit incumbents while lacking the multiplier-effect that a good strategy can deliver through bringing greater coherence and focus to policy objectives. Despite being over six months in preparation, with publication repeatedly delayed, the Green Paper has little discussion of the implicit tensions and conflicting demands that exist in policy making and provides little clarity on how regional rebalancing and sectoral deals will work in practice. It provides a long list of policy interventions but little by way of ground rules to provide a framework for future decision-making which, we would argue, should be the core of any long-term strategy. While we recognise that this is a Green Paper and the Government’s position is still developing, the weaknesses we have highlighted in this report leave us concerned that the Prime Minister has not yet been able to harness the political will across Government to truly drive forward her ambition and that the strategy will fall short of providing a clear framework for decision making in the long term.

We recommend that the Government reconsider giving sectoral strategies priority and instead focus on horizontal policies and specific ‘missions’ to meet UK-wide and local public policy challenges. This will make clear that the function of the Government’s industrial strategy—and of industry itself—is to solve societal problems and it will provide a clear focus for activity across Government and industry.

In conclusion, we urge the Government to continue to be ambitious developing its industrial strategy and ensuring that it remains true to the vision of achieving an economy that works for everyone.
1 Introduction

Our inquiry

1. In launching her bid to become Prime Minister and Leader of the Conservative Party, Theresa May spoke of her determination to introduce: “An economy that works for everyone, so we don’t just maintain economic confidence and steer the country through challenging times—but we make sure that everyone can share in the country’s wealth.” As part of this, she pledged to introduce: “A proper industrial strategy to get the whole economy firing.”

2. One of her first acts as Prime Minister was to create a new Department for Business, Energy and Industrial Strategy, which, among other things, was designed to develop “a long-term industrial strategy” as a means of improving the country’s competitiveness. This was the first time that “industrial strategy” had ever been included in a department’s title, and indicated the priority and strong intent of the new administration.

3. As the UK redefines its relationship with Europe and the rest of the world we have, in the Prime Minister’s words, “the opportunity […] to step back and ask ourselves what kind of country we want to be.” Our Report is intended to constructively contribute to the Government’s work on developing a new path for the country’s future by considering what kind of economy we should aspire to be and whether—and how—a new industrial strategy can help deliver this. Our Report is structured as follows:

   - Chapter 2 considers the economic challenges we face as a country and explains why we support the Prime Minister’s high-level vision for our future economic direction.
   - Chapter 3 outlines the design principles that we believe should underpin the Government’s new industrial strategy.
   - Chapter 4 looks at the need for strong horizontal policies that provide a robust foundation for future economic growth.
   - Chapter 5 looks in further detail at rebalancing our economy geographically and towards higher productivity industries.
   - Chapter 6 presents some final reflections on what we believe needs to happen next as Government continues to develop its strategy.

4. Our inquiry was launched in August 2016 and all of our evidence taking predated publication of the Government’s Industrial Strategy Green Paper on 23 January 2017. We are publishing our Report now, rather than gathering further evidence, to allow the Government to reflect on our recommendations alongside responses submitted to its Green Paper, as it continues to develop its thinking. We anticipate returning to this topic.

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1 Rt Hon Theresa May MP, Speech of 11 July 2016
2 Machinery of Government changes: Written Ministerial Statement (HCWS94), 18 July 2016
3 Rt Hon Theresa May MP, Speech of 17 January 2017
4 HM Government, Building our Industrial Strategy: Green Paper, January 2017
Interaction with other inquiries

5. This Report focuses on whether the Government’s proposed industrial strategy can help build a more equal, more productive, more competitive, more innovative and higher-skilled economy. It will be complemented over the coming months by three other major Reports into areas where we believe reform may be necessary to maintain and enhance our economic success following the vote to leave the European Union. Our inquiry into Corporate Governance will look at whether the Government has the right regulatory architecture in place to promote decision-making that creates sustainable, profitable companies which also look after their employee and wider stakeholder interests. Our inquiry into the Future World of Work will consider safeguards for employees in an age of increasingly precarious employment and given likely future changes that increased digitalisation and automation will bring. Our forthcoming inquiry into Scale-Up will determine how potential high-growth small businesses can be identified and supported to create disproportionately greater economic activity and employment.
A new vision for our economy

6. The vote to leave the European Union has created both a challenge and an opportunity for our society and our economy. Striking new trade deals and directly resuming responsibility for policies that were previously developed as part of our membership of the European Union means making choices that will shape and reflect the kind of nation we aspire to be in the future. As the Prime Minister has said, this is a time “to step back and ask ourselves what kind of country we want to be.”

7. In looking to set a vision for our future, the Prime Minister has explained that the Government’s “modern industrial strategy [...] will help to deliver a stronger economy and a fairer society—where wealth and opportunity are spread across every community in our United Kingdom.” The tone of her rhetoric, including to some extent the strong embrace of the term “industrial strategy”, strikes a significant departure from that of recent years, even decades. While the Cameron Government’s Productivity Plan focussed predominantly on improving our overall prosperity and growth as a nation, the Prime Minister has set an implicitly more redistributive mission, focussed not just on the size of the economy but on changing “the way our country works—and the people for whom it works—forever.”

The rationale for a new vision for our economy

Our economy does not currently work for everyone

8. It would be wrong and misleading to suggest that the UK does not have great economic successes. Our country is the fifth-biggest economy in the world. The UK is the world’s biggest net exporter of financial services. We are host to top international firms in professional and business services, including in advertising, accountancy, architecture, legal services and management consultancy. The UK’s Higher Education system is seen throughout the world as of exceptionally high quality, with three of the globe’s top ten universities being in this country. The UK pharmaceutical industry is the third largest in the world in terms of R&D intensity, and two UK companies in this sector are in the top ten globally for market share. UK aerospace is the second largest aerospace sector in the world, with 17 per cent of global market share. The UK automotive industry continues to go from strength to strength: 1.7 million cars were built in the UK last year, the highest output for almost two decades, with 80 per cent of production exported. The UK video games industry is the sixth largest market in the world; Grand Theft Auto V by Rockstar Games in the UK is the fastest selling entertainment product of all time, grossing $1bn worldwide in just 3 days. Five of the top ten selling musical artists in the world are

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5. Rt Hon Theresa May MP, Speech of 17 January 2017
7. As above.
8. World Bank GDP rankings accessed on 21 February 2017
9. “City leads UK to top spot among financial services exporters”, CityAM, 21 July 2015
11. BIS, The Pharmaceuticals Sector in the UK, 2010
14. ‘17 year high for British car manufacturing as global demand hits record levels’, SMMT, 26 January 2017
15. UKIE: The game industry in numbers, accessed on 21 February 2017
16. ‘Confirmed: Grand Theft Auto 5 breaks 6 sales world records’, Guinness World Records, 8 October 2013
British and one in six albums sold worldwide is by a British artist.\(^7\) This country should rightly be proud of these economic and industrial achievements, and be determined that our comparative advantage in these areas is maintained and enhanced in the face of severe international challenges and competition.

9. However, as the Prime Minister has recognised, the benefits of our economic success have not been felt by all. Analysis by the Equality Trust suggests that the UK became a much more equal nation during the post-war years but, from 1979, the process of narrowing inequality reversed sharply with inequality reaching a peak in 1990. Since then, and during a period of increased globalisation, inequality has stabilised but remained high.\(^8\)

10. Measured against the Gini coefficient, a commonly-used measure of income inequality, the UK has the second highest level of inequality in the G7, after the United States, and a Gini coefficient over 20 per cent higher than that for both Germany and France.\(^9\)

\[\text{Figure 1: UK Gini-coefficient 1961 to 2014–15}\]

Source: Institute for Fiscal Studies

11. The Industrial Strategy Green Paper recognises that 61 per cent of our population live in areas with incomes 10 per cent below the national average.\(^{10}\) Over the past fifteen years, gross disposable income per head outside of London has essentially flat-lined. The Equality Trust have found that while in 2014–15, households in the bottom 10 per cent of the population had on average a net income of £9,277, the top 10 per cent had net incomes over nine times that (£83,897). Inequality was much higher amongst original income than net income with the poorest 10 per cent having on average an original income of £4,467 whilst the top 10 per cent had an original income, 24 times larger (£107,597). Over time,

\(^7\) ‘One in six albums sold worldwide is by a UK star’, BBC News, 20 May 2016
\(^8\) ‘How Has Inequality Change’, The Equality Trust, accessed on 21 February 2017
\(^9\) BEIS Committee analysis of OECD data
\(^{10}\) HM Government, Building our Industrial Strategy: Green Paper, January 2017, p.13
rising inequality has seen a dramatic increase in the share of income going to the top, a decline in the share of those at the bottom and, more recently, a stagnation of incomes among those in the middle.\textsuperscript{21}

**Figure 2: Changes in income for highest earners in the UK 1990–2012**

![Chart showing changes in income for highest earners in the UK 1990–2012](chart.png)

Source: The Equality Trust

12. While headline economic growth rebounded following the 2007 financial crisis, that growth has by no means been felt evenly. As the Chief Economist of the Bank of England, Andrew Haldane, has explained, “Half of all UK households have seen no material recovery in their real disposable incomes since around 2005. Or, put more provocatively, the majority of UK households have faced a ‘lost decade’ of income.”\textsuperscript{22} Haldane’s commentary highlights a range of further inequalities too, including:

- Slight reductions in the income gap between the richest and poorest have also been accompanied by a growing wealth gap, with the poorest quintile of the population experiencing a fall in wealth while the richest quintile have experienced a 20 per cent increase in wealth since 2010.\textsuperscript{23}

- Overall reductions in the unemployment rate have been accompanied by a significant increase in the number of people who are self-employed or on zero-hours contracts, a significant proportion of whom would prefer less precarious employment or more hours.\textsuperscript{24}

- There is a growing inter-generational gap in income. Nominal earnings of those under-30 have risen by a cumulative 6 per cent since 2007, while those over-50 have seen cumulative gains of 22 per cent.

\textsuperscript{21} As above.
\textsuperscript{22} Andrew Haldane, *Speech of 30 June 2016*, Bank of England
\textsuperscript{23} As above.
\textsuperscript{24} As above. Around 15 per cent of those working part-time would prefer to be in full-time employment. And around a third of those on temporary contracts would prefer to be on permanent contracts.
Headline economic success masks significant weaknesses

13. While recognising the UK’s economic strengths, the Industrial Strategy Green Paper also provides a detailed—and refreshingly honest—analysis of our economic weaknesses. We will not rehearse these at length but, to summarise they include:

- **The UK has low labour productivity than comparable economies.** UK labour productivity was 18 per cent below the G7 average in 2015, the largest gap since at least 1991; and, UK productivity has been below that of the United States, France and Germany since the mid-1970s.  

Figure 4: Constant price GDP per hour worked, actuals and projections 1997 to 2015

Source: [OECD, Office for National Statistics](#)
• The UK has some of the worst basic numeracy and literacy rates in the OECD.\textsuperscript{26} Only 10 per cent of adults hold technical education as their highest qualification, placing us 16th out of 20 OECD countries,\textsuperscript{27} and we are forecast to slip even further down the OECD rankings.\textsuperscript{28}

• Despite having the world’s fifth largest economy, the UK is currently ranked 24th in the world for the quality of its infrastructure.\textsuperscript{29} Successive governments over many decades have failed to prioritise infrastructure investment, and this neglect has undoubtedly contributed to the UK’s long-term poor productivity performance. As a share of GDP, investment on physical infrastructure in the UK has ranked in the lowest 25 per cent of OECD countries for 48 of the last 55 years, and the lowest 10 per cent for 16 of the last 21 years.\textsuperscript{30} Our digital infrastructure also performs relatively poorly. The UK ranks globally 23rd in average download speeds and an even lower 48th in upload speeds.\textsuperscript{31}

• The UK’s R&D intensity (R&D spend as a proportion of GDP) has declined over the years—in a study of ten countries, the UK was the only country which saw its R&D intensity fall between the periods 1991–1995 and 2006–2010.\textsuperscript{32} Total R&D expenditure in 2014 represented 1.67 per cent of GDP. UK gross domestic R&D expenditure, as a percentage of GDP, declined steadily between 1990 and 1997. Since 1998, the level has fluctuated between 1.59 per cent and 1.73 per cent with an average estimate of 1.67 per cent for the period 1998 to 2014.\textsuperscript{33}

Figure 5: UK gross expenditure on R&D as a percentage of GDP, 1990 to 2014

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\caption{UK gross expenditure on R&D as a percentage of GDP, 1990 to 2014}
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\begin{flushright}
Source: Office for National Statistics
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\textsuperscript{26} OECD, Building Skills for All: A review of England, 2016
\textsuperscript{27} HM Government, Building our Industrial Strategy: Green Paper, January 2017, p. 38
\textsuperscript{28} HM Treasury, Fixing the Foundations: Creating a more prosperous nation, July 2015
\textsuperscript{29} CBI, Think Globally, Delivering Locally, November 2016
\textsuperscript{30} HM Treasury, Fixing the Foundations: Creating a more prosperous nation, July 2015
\textsuperscript{31} Institute of Directors (ISG0025)
\textsuperscript{32} BIS, International industrial policy experiences and the lessons for the UK, 2013
\textsuperscript{33} Office for National Statistics, UK Gross domestic expenditure on research and development: 2014
\end{flushleft}
• The UK lags behind other countries in the extent to which our companies scale-up, with research suggesting that many of our companies have stagnant growth despite their best aspirations.\textsuperscript{34} The Industrial Strategy Green Paper highlights OECD research which found that while we rank third for start-ups, we rank 13th for the number of businesses that scale up successfully.\textsuperscript{35}

• The UK suffers from a long-standing trade deficit. Despite being the second largest exporter of services and the ninth largest exporter of goods in the world,\textsuperscript{36} our balance of trade has been in deficit since the mid-1980s.\textsuperscript{37} The growth of UK exports has been particularly weak since the 2008 financial crisis despite the steep fall in the value of sterling, which should have boosted exports, with the UK experiencing the slowest annual growth rate in exports of all G7 countries.\textsuperscript{38} Based on average growth rates in exports from 2010–2014, the Government is likely to fall far short of its target of increasing the value of exports to £1 trillion by 2020.

• The UK has significant regional disparities not only in income but also in productivity, skills, and infrastructure investment. London and the South East are the only parts of the UK to experience above average productivity; public spending per head on infrastructure and research varies widely across the country, as does the proportion of the local population with higher level qualifications.

14. We commend the Government for its honesty in its analysis of the UK economy’s structural weaknesses. However, it is also fair to say that the Industrial Strategy Green Paper is the latest in a long line of Government-commissioned documents, stretching back many decades, which has identified shortcomings in the UK’s economic performance on matters like low productivity, insufficient investment in infrastructure and R&D, skills deficiencies and poor export performance. As Prime Minister in the early 1960s, Harold Macmillan wrote a paper to his Cabinet, stating:

“\textquote{We have now reached a stage in our post-war history where some more radical attack must be made upon the weaknesses of our economy, both productive and structural. We face a situation in which the conditions of trade are becoming increasingly competitive and our commercial rivals increasingly better equipped to compete with us, while our own economy remains sluggish and ‘patchy’ … in order to enhance our competitive power … we have to increase our productivity by bringing our productive capacity into full use, by eliminating restrictive practices and by developing to the utmost the new methods which technology is bringing within our reach. Whatever the result of the Brussels negotiations, this need is urgent. In or out of Europe, Britain needs to be brought up to date in almost every sphere of life. Second, we have to re-organise the structure of the island in

\textsuperscript{34} Sherry Coutu CBE, \textit{The Scale Up Report on UK Economic Growth}, November 2014
\textsuperscript{36} WTO, \textit{World Trade Statistical Review 2016} accessed 8 February 2017
\textsuperscript{37} BEIS Committee analysis of OECD data
\textsuperscript{38} BEIS Committee analysis of OECD data
such a way as to rectify the imbalance between south and north—between the ‘rich’ areas and the ‘poor’ regions, the over-employed regions and the under-employed regions—and redress the grave social anomalies which are created by this imbalance”.39

Such sentiment was the rationale behind the creation of the National Economic Development Committee (‘Neddy’), indicative planning between government, employers and trade unions which set an overall growth rate target of 4 per cent per annum, as well as growth and investment targets for specific industrial sectors.

**Global economic change**

15. While the Industrial Strategy Green Paper primarily focuses on the domestic economic challenges, it is important to recognise that the global economy is currently facing a wholesale period of transformation, for instance:

- The need to decarbonise in order to manage and mitigate the risks of climate change will have profound implications for the way we produce and consume not only energy but also goods and services;
- The fourth industrial revolution is expected to radically change how businesses operate and the types of work that are available in the future; and,
- Changing demographics and an ageing population in many countries will challenge our ability to maintain future living standards.

As the Secretary of State for Business, Energy and Industrial Strategy put it: “The times that we are living in—not just post Brexit when we do need to set out how we are going to compete in the future, but with the development of technology around the world—are posing big challenges.”40

**Setting a new direction**

16. In recognising the extent to which economic growth has failed to trickle down to many households and describing the causes of our poor productivity, the Government has provided a compelling argument for change. The Green Paper outlines deeply embedded weaknesses within the UK’s economy that have remained unresolved by successive governments. The UK’s headline economic success in recent decades has been felt by too few and its foundations are shallow. As a country, we have not invested enough in infrastructure or innovation, and our skills-levels remain poor despite significant spending. Too many people in too many parts of the country have not felt the benefits of growth.

17. We strongly welcome and endorse the Prime Minister’s aspiration of “an economy that works for everyone”. The ultimate test of Government’s success in delivering this will be whether we see increased living standards across society and a reversal in the trend of widening gaps in the distribution of income and wealth.

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40 Oral evidence taken on 14 December 2016, [HC (2016–17) 566](https://www.parliament.uk/), Q103
18. We agree with the Government’s vision that we should aspire towards an economy which is more productive and where the benefits of growth are felt more evenly throughout the UK. To this we would add that a further objective should be to ensure that the UK economy is fit to face the global challenges and opportunities of our age such as: the technological changes brought about through the fourth industrial revolution, and the challenges these will present for the labour market; changing demographics and an ageing population; and, the pressing need for decarbonisation.

19. Successive governments over many decades have correctly identified long-term challenges and weaknesses within the UK’s economy on matters like poor productivity, skills deficiencies, inadequate investment on infrastructure and low spending on research and development. However, few administrations have had unqualified successes and many have spent huge amounts of taxpayers money in failing to address these weaknesses. While the Prime Minister’s rhetoric suggests an intention to approach this with a welcome and renewed vigour, the incremental proposals outlined in the Green Paper leave us sceptical about whether the fresh thinking or political will is present across Government to deliver the Prime Minister’s objectives.

The role of industrial strategy

20. Having an industrial strategy does not suggest that a country is moving away from a belief in the power of markets. On the contrary, in the modern global economy, strategic state support for business growth and economic goals is the norm, not the exception. While, anecdotally, current European Union rules around State Aid are often cited by officials as a reason for a lack of public sector intervention and support in the UK, EU data makes clear that many other economies in Europe—including Germany and France (the fourth and sixth biggest economies in the world, respectively)\textsuperscript{41}—spend a considerably higher proportion of their GDP on State Aid than the UK does. In fact, out of other European Union member States, only Italy, Spain and Denmark spend a lower proportion of GDP on State Aid than the UK does.

\textsuperscript{41} International Monetary Fund, \textit{World Economic Outlook Database}, accessed 8 February 2017
21. That said, the term “industrial strategy” has a chequered history in the UK that can provoke strong reactions. The perceived failure of industrial strategy in the 1960s and 1970s led to the phrase being associated with the assumption “that government could act as a backstop for the decline of ever more uncompetitive industries in an increasingly globalised commercial landscape.”

22. The concept of an explicit industrial strategy was resurrected by the Labour Government following the 2008 financial crisis, under the term “industrial activism” and evolved further under the Coalition Government, before experiencing a brief “hiatus” after the May 2015 election. This approach sought to differentiate itself from that of the 1960s and 1970s by espousing a philosophy of working with the grain of markets and competition. For the Institute of Directors, modern industrial strategy “is a strategy...”

Source: Eurostat

42 Institute of Directors (ISG0025)
43 Q351 [Lord Mandelson]
not centred on ‘picking winners’ in the traditional sense, but rather on the government championing new, innovative industries through vocal support, tax incentives for investors, research funding, and a hands off regulatory approach.” Or, as the Coalition Government described it, industrial strategy is “the whole of government working in partnership with industry to set the long term direction needed to give business the confidence to invest [and] to create more opportunities, skilled jobs and to make the UK more competitive so British businesses can thrive and compete with rising economies.”

This sentiment has been echoed in the Industrial Strategy Green Paper.

23. The Prime Minister’s rhetoric on industrial strategy marks a significant step change from that in recent years, as signified by the creation of a new department with the term in its title. However, to some extent application of the term “industrial strategy” to existing policies is arbitrary and, while the rhetoric is apparently radical, the Government’s approach appears to be evolutionary. For instance, while the former Business Secretary, the Rt Hon Sajid Javid MP, said he preferred the term “industrial approach”, in practice what he described doing is little different to the sectoral approach that his successor is proposing:

Rt Hon Sajid Javid MP, March 2016—”I’ve taken the old strategy’s closed shop and replaced it with an open door. A willingness to deal with representatives of all sectors and to respond positively to industry-led solutions.”

Industrial Strategy Green Paper, January 2017—”We propose to set an ‘open door’ challenge to industry to come to Government with proposals to transform their sectors through ‘Sector Deals’.”

Likewise, the Green Paper’s focus on regional growth and horizontal policies expands on themes set out in the Government’s previous productivity plan. Where the May Government’s approach to “industrial strategy” differs is that it suggests a more explicit and conscious approach to coordinating Government policies at both a national and local level and, coupled with recent funding announcements, suggests that Government intends to pursue its objectives with greater vigour than was previously the case.

**What does having an industrial strategy mean in practice?**

24. Evidence to our inquiry was wide ranging and included many different suggestions as to what approach Government’s industrial strategy should take. Much of the evidence we received included suggestions from particular sectors about ways in which Government could reduce or amend regulation and taxation or provide particular incentives and support to help them grow.

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44 Institute of Directors (ISG0025)
45 BIS, _Industrial strategy: government and industry in partnership_, August 2013
47 “Sajid Javid heralds Thatcherite approach to business policy”, _Financial Times_, 16 September 2015
48 Rt Hon Sajid Javid MP, _Speech of 3 March 2016_
50 HM Treasury, _Fixing the Foundations_, July 2015
25. During our inquiry we heard that industrial strategy should be seen as “a framework within which a country can think about how it supports those aspects of industry for which either it has great opportunity or great need”, and that:

“Industrial strategy is [ … ] not about goals, objectives or picking winners. Nor is it rebranded industrial policy. Instead it involves diagnosing problems, a process of analysing and choosing an appropriate set of policies that reinforce each other (within a given context), to deliver desired objectives.”

26. Fundamentally, the vast majority of respondents to our inquiry welcomed the Government’s revived interest in industrial strategy explicitly, or more frequently implicitly, on the grounds that:

a) There are barriers to growth and market failures that Government intervention is considered necessary to overcome; and,

b) Government policy choices inherently have an economic impact and these should be coordinated and driven by a consideration of longer-term objectives and priorities (though views on what those should be inevitably differ).

27. Finally, and particularly in the context of the UK’s decision to leave the EU, industrial strategy can, in the words of the CBI, become a “calling card” for the UK’s economy in the world, mitigating uncertainty by setting out clearly our ambitions and plans for the world-class infrastructure, innovation and skills that will ensure that the UK remains at the heart of the global economy.

28. The wide range of responses we received to our inquiry reflects the fact that the country faces choices about how it would like to see its economy develop in the future, the kinds of safeguards it would like to put in place, and the extent to which it believes that different types of intervention (or an absence of intervention) will best deliver its economic vision and help different industries to thrive. Contributors to our inquiry have seen it as a framework for coordinating the Government’s economic policies and interventions towards a defined objective or set of objectives.

29. An explicit industrial strategy recognises that many Government policies inherently have an impact on the different sectors, nations and regions that comprise the UK’s economy. We have a choice as to whether these policies are implemented in an incoherent, ad hoc manner or work together toward a clear vision of the kind of economy we want. As the Prime Minister has recognised, an industrial strategy can provide a ‘practical and proactive’ framework for government intervention that can help address our economic weaknesses and ensure that our economy works for everyone.

30. The remainder of this Report looks at the principles that we believe need to underpin a successful industrial strategy, and some of the key issues that will need to be tackled in its delivery.

51 Q225 [Dr Celia Caulcott]
52 Professor Paul Nightingale (ISG0134)
53 For example: Royal Aeronautical Society (ISG0145); ICAEW (ISG0183); Aerospace Technology Institute (ISG0037)
54 For example: Sheffield Political Economy Research Institute (ISG0057); Q295 [Paul Nowak]; Q423 [Andrew Lewis]; CF Fertilisers (ISG0082)
55 Confederation of British Industry (ISG0133)
3 Principles for an effective industrial strategy

31. The Secretary of State has said that the Government’s industrial strategy aims “to provide a policy framework against which major public and private investment decisions can be made with confidence,” and that the purpose of the Green Paper is to help develop this framework collaboratively. Evidence to our inquiry has led us to conclude that such a framework needs to be underpinned by some clear design principles. These principles, and the extent to which the proposals in the Green Paper align with them, are discussed in further detail below. To summarise, in our view, an effective industrial strategy needs:

(1) Clear objectives, with progress measured against meaningful metrics;

(2) A ‘mission-based’ approach, shaped by a vision as to the direction we want the economy to move towards, underpinned by a foundation of strong horizontal policies;

(3) To ensure that all relevant Government departments and devolved administrations work effectively together to reconcile policy tensions and contribute fully to the delivery of industrial strategy;

(4) To be long-term in its approach, transcending parliaments and individual administrations, and developed in close collaboration with the full breadth of economic actors and with sensitivity to geography, to ensure that it endures;

(5) To be simple, accessible and understandable to business across the economy, including small and medium-sized enterprises (SMEs) and supply-chains;

(6) To be clear that, painful though this may be, it should not provide palliative care for failing and obsolete industries; and,

(7) To retain the flexibility to act pragmatically according to events.

Clear objectives measured against meaningful metrics

Ensuring objectives are coherent and aligned with goals

32. A strategy is not a static document but an evolving process that works towards a clearly defined goal; its core purpose is to identify the critical factors that need to be addressed to achieve that goal and then design a way of coordinating and focusing action to address those factors.

33. The Government has stated that the objective of its industrial strategy is: “to improve living standards and economic growth by increasing productivity and driving growth across the whole country.” In doing this it has said that its industrial strategy must:

- Build on our strengths and extend excellence into the future;

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• Close the gap between the UK’s most productive companies, industries, places and people, and the rest; and

• Make the UK one of the most competitive places in the world to start or grow a business.  

34. All of these are sensible overarching aims and we welcome them. However, there are implicit tensions between these objectives. We heard that one weakness of previous strategies is that they have not given clarity about how to prioritise ‘horizontal’ policy decisions, and it is not clear to us how the objectives for the industrial strategy provide a framework for wider policy making or addressing policy trade-offs or contradictions. For instance, building on our economic strengths could imply supporting the most productive industries and regions, but this would not necessarily help close the “gap” with less productive companies.

35. The only objective of the industrial strategy which directly aligns with the Prime Minister’s vision is the ambition to close the productivity gap between the UK’s companies, nations and regions. It is entirely conceivable that Government could develop policies to “build on our strengths” and make the UK “one of the most competitive places” to start or grow a business without addressing the regional disparities that the Prime Minister has spoken so strongly about addressing.

36. In this context, it is important to understand how the Government sees the specific objectives and policies of the industrial strategy aligning with the Prime Minister’s overall goal of an economy that works for all. The Government also needs to provide clarity on to what extent, if any, other forthcoming strategies and policies are intended to contribute to that end.

37. The Prime Minister’s rhetoric marks a significant shift away from that of previous Governments; consciously or unconsciously, it implies that the Government is willing to exchange headline economic growth for more evenly distributed and resilient growth. At a time when Government is already having problems in balancing the books, any decision to sacrifice some element of short-term economic growth for other objectives (with a longer-term return) will make that task more difficult. We would welcome clarity as to whether this is the right way to interpret her remarks. Success will only be achieved if policies are of a scale to match the Government’s ambition and clearly drive forward economic rebalancing.

Meaningful metrics are necessary to assess progress

38. As the adage goes, ‘what gets measured gets managed’, having clear metrics can help galvanise and focus action. Giving evidence to us, the Secretary of State expressed his reluctance to give a “round number […] just for the purpose of setting out an approach,” and we appreciate that arbitrary targets are unhelpful. However, clearly articulated targets are necessary to ensure Government and industry are able to align in the same direction and to build a sense of common purpose. As the Confederation of British Industry (CBI) told us, “To deliver effective industrial strategy, all departments, agencies and levels of
government should share common industrial strategy goals.” It is hard to comprehend how policies can be designed to deliver a strategy in the absence of a clearly articulated and measurable set of outcomes, even if those will necessarily be high-level. As the EEF – the Manufacturers’ Organisation wrote in evidence, one of the main components of any industrial strategy has to be “A clear sense of economic outcomes, with measures that ensure progress can be monitored and acted upon.”

39. In developing metrics against which to assess the impact of the industrial strategy, we hope that lessons are learned from our Report on the Productivity Plan, in which we expressed concern about the lack of metrics for success. We are grateful that the Government’s response to our Report included a very useful and detailed annex listing progress against commitments and detailed “success metrics”, but we are not convinced that all of the metrics are sufficiently meaningful and outcomes-focussed. For instance, having a target of the lowest rate of corporation tax in the G20 is solely a measure of policy inputs, not of outcomes.

40. Another example relates to the Productivity Plan’s objective of having “World-class digital infrastructure in every part of the UK.” One of the measures of success, the percentage of UK premises with 4G coverage from at least one operator, sounds impressive on the face of it, with the latest figure standing at 97.8 per cent. However, this inputs-based metric is a questionable measure of success given that the National Infrastructure Commission has found that Britain is 54th in the world for 4G, with the typical user only able to access 4G 53 per cent of the time. This is a clear example where Government has defined “success” on its own terms, rather than in a way which reflects the real experiences of the UK’s businesses and citizens, just as pronouncements on the UK’s overall economic growth have previously disguised the fact that too many people have not felt the benefits of this.

41. We do not expect the Government to commit to arbitrary targets, but it should produce a set of measures against which it will be possible to assess whether progress is being made towards delivering an economy that works for everyone. In its response to this Report, the Government should outline a set of clear, outcomes-focussed metrics that can be used to frame its goals and to measure progress in meeting these. We recommend that the Government should consider including metrics relating to the following:

- *Improving in real-terms earnings per household and closing regional disparities;*
- *Reducing differential regional GDP per head between least and best performing nations and regions;*
- *Improving UK productivity relative to comparator economies and closing the gap with the G7 average;*

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62 CBI (ISG0133)
63 EEF (ISG0067)
• Improving UK Gross Domestic Expenditure on R&D relative to comparative OECD economies;

• Improving levels of UK investment in fixed capital relative to comparable OECD economies;

• Improving the UK’s position in international rankings on basic skills;

• Improving the UK’s position in international rankings on infrastructure;

• Ensuring emissions remain within Carbon Budgets and legal limits for air pollution;

• Closing the UK trade deficit; and,

• Improving the proportion of businesses which scale-up.

42. While we recognise that information on all of these is already regularly published by different Government bodies such as the Office for Budget Responsibility and the Office of National Statistics, we believe that it would be helpful to bring them together in a single annual report to Parliament, with a debate on industrial strategy becoming a regular and established part of the Parliamentary calendar. Such a report could also include updates on commitments being delivered to implement the industrial strategy and any new commitments made as the strategy evolves over time, recognising that strategy is “a process, not an event.” It would also be helpful for the Government to publish details of any interim updates on statistics in the same place on GOV.UK, providing a clear dashboard of measures through which Parliament and the wider public could hold the Government to account for delivery.

43. As the Government develops the detailed policies that work towards its overarching vision and goals, we anticipate that it will develop more detailed commitments and interventions. We recommend that the Government publishes annual updates to its action plan outlining progress in delivering policies and setting out any new policies and how they align with the overall strategy. The Government should also create a single dashboard of metrics relating to industrial strategy on GOV.UK which should be updated as new statistics are published.

44. Together, these measures would demonstrably show a commitment to ensuring transparency and accountability.

A ‘mission-based approach’ underpinned by strong horizontal policies

The need for strong horizontal policies

45. The Government’s approach to industrial strategy places a strong focus on horizontal policies, coupled with deeper, sectoral interventions.
Table 1: Analysis of the 10 pillars of Government’s industrial strategy by type of intervention

<table>
<thead>
<tr>
<th>Horizontal Pillars</th>
<th>Sectoral Pillars</th>
</tr>
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<tbody>
<tr>
<td>- Investing in science and research</td>
<td>- Cultivating world-leading sectors</td>
</tr>
<tr>
<td>- Developing skills</td>
<td>- Supporting energy innovation</td>
</tr>
<tr>
<td>- Upgrading infrastructure</td>
<td></td>
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<tr>
<td>- Business support</td>
<td></td>
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<tr>
<td>- Improving procurement</td>
<td></td>
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<tr>
<td>- Encouraging trade and investment</td>
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<tr>
<td>-Creating the right institutions</td>
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<tr>
<td>- Delivering affordable energy</td>
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Source: BEIS Committee Analysis

46. As the Secretary of State told us, “a lot of the meat of what we need to do is quite cross cutting and will affect things, whether it is science and research and innovation, whether it is education and training, whether it is infrastructure; it will cover a lot of different sectors”.69 This focus on strengthening horizontal policies was widely supported in evidence to us. As the CBI have commented, horizontal policies such as these are essential precursors and enabling factors that form “the bedrock on which a successful industrial strategy is built” and “enable and incentivise all businesses to undertake activities central to realisation of the UK’s industrial potential.”70

47. However, as both the CBI’s submission to our inquiry and the Secretary of State’s approach make clear, horizontal policies alone do not amount to the totality of an industrial strategy. Being on the front foot in responding to the changing nature of work, emerging technologies, and climate change, for instance, will require a more focussed response than broad-brush horizontal policies. While a small number of submissions to our inquiry suggested that Government should focus solely on horizontal approaches,71 the majority called for these to be complemented by deeper interventions, whether those be to support specific sectors or missions. Although not an advocate of industrial strategy themselves, as the Institute of Economics Affairs commented, a “horizontal industrial strategy [...] is just an economic policy [...] not worthy of the name industrial strategy.”72 We very much agree with this assessment.

48. The Government’s Green Paper has emphasised the importance of horizontal policies, including improving investment in: research and development, upgrading our performance on education and skills, and upgrading the quality of our infrastructure, procurement policy, trade and investment, clean growth, and business support. Horizontal policies form the backbone of effective industrial policy. However, as the Government has recognised, they alone seem unlikely to deliver the Secretary of State’s larger ambition of getting to grips with “the problems and opportunities that we face over the next 10, 15 or 20 years.”

69 Q105
70 CBI (ISG0133)
71 Institute of Economic Affairs (ISG0045)
72 Q302
Sector-based interventions

49. The Industrial Strategy Green Paper places an emphasis on cultivating “world-leading sectors” through sectoral “deals”. This deeper and more proactive form of intervention is what takes the Government’s proposals beyond economic policy and into the realms of industrial strategy. These are what the CBI sees as being at the higher end of Government intervention.

50. A substantial body of evidence we received related to specific sectors calling for recognition as part of a new industrial strategy, ranging from the financial technologies industry, and professional services, through to hospitality and tourism. Major business umbrella organisations, including the CBI and the EEF also called on the Government’s industrial strategy to take a sector-led approach that, in the words of the CBI, “seeks to capitalise on areas of the economy in which the UK has a competitive advantage.” Arguments supporting sector-based interventions are frequently and understandably made on the grounds that each sector has unique needs and playing an important role in the economy: “The needs of financial services are different from aerospace which differ in turn from life sciences.” We have particularly heard that long-term sectoral support for the automotive and aerospace industries has helped them flourish; however, it has also been pointed out that the sectoral approach promoted under the Coalition Government did not necessarily prove successful for other sectors, such as construction. It was also unclear as to how the eleven sectors adopted as the Coalition Government’s industrial strategy were chosen, to the exclusion of other important sectors, such as the creative industries.

51. We recognise that specific industries are likely to have particular asks of Government, and that sectors are a natural way for many businesses to coordinate and organise. We do not necessarily disagree with this approach, although we also believe there is a significant risk that it can lead to capture by private lobbying interests. We heard claims in evidence that “some of the most regressive and problematic tax policy in this country has been lobbied for by particular companies in the name of innovation. That is capture and it wastes a lot of public money.”

52. While recognising that many sectors perhaps naturally favour sector-specific strategies, we have also heard strong arguments against a sectoral approach. A range of witnesses have cautioned that information imbalances and competing priorities can lead to poor decision-making in Government: “mistakes in the past have been made in part because dialogue with the private sector on industrial strategy is not always easy: companies have competing interests, influence and priorities.” Evidence against adopting a sectoral approach argued that it can be bureaucratic, that benefits are not felt

74 Confederation of British Industry ([SG0133](#))
75 MasterCard ([SG0044](#))
76 ICAEW ([SG0183](#))
77 British Hospitality Association ([SG0073](#))
78 Confederation of British Industry ([SG0133](#))
79 Novartis ([SG0077](#))
80 Q308 [Paul Nowak]
81 Q103 [Professor David Greenwood]
82 Q311 [Professor Mariana Mazzucato]
83 ARM Holdings ([SG0009](#))
84 Solent Deal Authorities ([SG0010](#))
by the wider economy,\(^{85}\) and that, at worst, a siloed approach can have an adverse impact on other parts of the economy.\(^{86}\) A number of witnesses argued that innovation occurs at the boundaries between sectors,\(^{87}\) and noted that many businesses, particularly in supply-chains, do not neatly fit in to specific sectoral categories.\(^{88}\) It is not clear how spill-over effects can be maximised if a stricter sector-based vertical approach was adopted. Our nation’s strength in creative industries, particularly design, for example, will undoubtedly have a positive impact upon producing new products and processes in manufacturing.

53. Although we frequently heard evidence that successive Governments’ support for the automotive and aerospace sectors had helped them flourish, we note that the Government has described these as having “unique characteristics that warrant particular support being provided”.\(^{89}\) We have also heard that the benefits of a sectoral approach were less clear for many of the other sectors. We heard for instance, that previous sectoral strategies had lacked “operational detail”,\(^{90}\) and that while elements of some sectoral plans had been delivered successfully, they had not necessarily had the clear leadership and broader industry support necessary to ensure benefits were fully realised.\(^{91}\) Essentially, “approaches where specific sectors are targeted have not always delivered the strongest results”\(^{92}\) with some sectoral strategies having set overarching visions but been “less successful in terms of moving beyond that to concrete actions that have delivered measurable progress.”\(^{93}\)

54. **Sectoral policies appear to have worked well for the automotive and aerospace industries.** However, with regards to other sectors this approach has had, at best, mixed results. Furthermore, this approach appears to have the greatest risk of policy being built on the vested interests of big businesses and incumbents that are best equipped to lobby. Despite Government allowing sectors to self-identify, there is a risk that a sectoral approach encourages businesses to maintain rather than break down silos, and leads to policies designed to suit preferred industries at the expense of other sectors and the wider public interest.

55. *We recommend that Government reconsider giving sectoral strategies priority and instead focus on horizontal policies and specific ‘missions’ to meet UK-wide and local public policy challenges.*

**Early sectoral deals**

56. The Industrial Strategy Green Paper announces that work is underway on a number of early sector deals covering: life sciences, ultra-low emission vehicles, industrial digitalisation, nuclear and creative industries. We do not question the importance of these areas of the UK economy, but it is unclear why they appear to have been given a privileged status in the Green Paper or how they were chosen to spearhead implementation of this approach. Use of the term ‘sectors’ is also unhelpful—arguably the ultra-low emission vehicles industry is increasingly well established and is a product rather than a sector,
“industrial digitalisation” is a vague term that could cover many things, and the “creative industries” is likewise hugely diverse. In the absence of a clear set of criteria for “deals”, there is a real risk that engagement lacks focus and leads to talking-shops rather than meaningful results with a real transformative potential. The suggestion that industries need to “organise behind strong leadership” and the naming of key individuals to lead different deals,\(^{94}\) risks creating a cult of personality where individual leaders come to the fore at the expense of areas where a potentially greater impact could be had. Given the Government’s on-going positive support for the aerospace industry, it is curious that this sector is not also included and highlights the limitations of choosing, in an arbitrary way, specific sectors.

57. In its response to this Report, the Government should set out the process by which it agreed to prioritise “deals” with the five sectors listed in the Industrial Strategy Green Paper, whether it held discussions with any other sectors about doing ‘deals’ and, if so, why those “deals” were not progressed at this time or referred to in the Green Paper. The Government also needs to clarify how it will evaluate future sectoral definitions, priorities and targets if it continues to pursue sectoral deals.

**Mission-based interventions**

58. Although the Government has signalled that it intends to take a sectoral approach, we believe that some of the risks outlined above, particularly around special pleading, could be mitigated by adopting a ‘mission-based’ approach, whereby Government support for deeper industrial interventions is focussed on addressing particular public policy challenges. In essence, “an industrial strategy need not have a sector-by-sector focus in order to deliver benefits. Instead, it may set out the objectives that the economy should deliver, and leave it to industries to respond to the challenge.”\(^{95}\)

59. This challenge and the benefits of a mission-based approach were summarised particularly clearly in evidence from the University of Sussex Science Policy Research Unit:

> “Past UK industrial strategies have tended to default towards a sectoral approach. There are good reasons for this, as sectors offer a good organizing basis for solving coordination problems related to, for example, skills. But there are also risks to a sectoral approach, such as capture to private lobbying interests […] This is where instead of driving to the frontier of new ideas, firms influence governmental programmes and policy making. Starting with problems, not sectors, helps to minimise this problem.”\(^{96}\)

60. A mission-based approach was also warmly endorsed by the British Chambers of Commerce, who told us that “setting a series of national goals or missions that galvanise public and cross-political support could boost new industrial development.”\(^{97}\) It was also backed by the Government’s own innovation agency, Innovate UK, which saw a mission-based approach as a “strong driver” for tackling the country’s productivity problem and enabling actors from multiple-sectors “to work in a common direction for the highest

\(^{95}\) British Property Federation (ISG0042)
\(^{96}\) SPRU (ISG0111)
\(^{97}\) British Chambers of Commerce (ISG0181)
societal benefit.” Linked to this, we heard evidence that a mission-based approach could help build the broad-based support necessary for a long-term industrial strategy by recognising that economic growth has a “direction” as well as a “rate” and seeking to harness this towards societal outcomes.

61. There are some positive examples of Government leaning towards this approach in its Industrial Strategy Green Paper—for instance, the announcement of a strategy with a clear aim to support the transition to ultra-low emissions vehicles. However, other early announcements on sectoral strategies lack this level of focus. The Government’s proposal that new sector “deals” should be targeted at addressing “sector-specific challenges” does go some way towards our mission-based industrial strategy but it is important that those “challenges” are focussed clearly on societal goals, and long-term economic goals.

62. Such an approach requires a vision for the economy. The Prime Minister has arguably made a good start with “an economy that works for everyone”. However, this strapline now needs to be translated into more detailed policies to enable this objective to be achieved.

“One thing that comes out strongly through the review of industrial experiences in other countries is the importance of the national vision. If Hamilton’s vision that his country can one day become a powerful industrial nation, like Britain, lost out to Jefferson’s vision, harking back to the days of yeoman farmers, the US may have remained a richer version of Argentina today. Without Japan daring to dream that one day it will beat the Americans in the car industry (in 1955, the US produced 7 million cars, against 70,000 for Japan), we would have had no Toyota, and its luxury brand, Lexus. If Finland—a tiny nation of 3–4 million people with seven centuries of colonial history—did not aspire to compete in the most difficult industries with the best nations in the world, it would have maintained its specialisation in logging—not an easy thing to avoid, when you have one of the largest endowments of timber per capita in the world. Without China—one of the poorest nations in the world—believing itself to be capable of becoming the next superpower (which may or may not come true), its industrial policy efforts would have been much less ambitious than what it has been and the result of it much more modest. And so on.”

63. Whereas a sector based approach is essentially another form of “picking winners”, a mission-based approach provides a means of articulating a positive economic vision and picking public policy challenges and allowing all sectors to put forward contributions to solving these.

64. We recommend that specific support for industry be guided by a targeted ‘mission-based’ approach, channelling the Government’s support towards addressing the big challenges of the future. It is for Government to set those missions, in discussion with stakeholders. Examples could include decarbonising our energy intensive industries, improving the affordability and effectiveness of health and social care in the context of an ageing population, maximising the country’s opportunities arising from the fourth...
industrial revolution, automating and electrifying our transport infrastructure, or capturing as much value from a growing global population with rising disposable income which wishes to travel, be educated and be entertained.

65. “Missions” need not be inconsistent with the Secretary of State’s vision of deals focussed on sectoral challenges. Rather, any such “deals” need a clear, time-bound goal. Furthermore, clear criteria are needed to decide which challenges are worth pursuing and which are not. Missions could provide a useful framework for setting those criteria.

A genuinely whole of Government approach

66. Over the course of our inquiry we heard a recognition from former Ministers that there are “inherent tensions” between government objectives, coupled with a frustration from business that often Government policies are not coherent and decisions made by one part of Government may be “undermined by decisions in other parts of Government.”

For example, we heard from university-sector representatives that the ambition to grow education exports could clash with goals on immigration. Many witnesses saw industrial strategy as a vehicle to “link all Departments for a common purpose.” We think this is an admirable approach for the Government to pursue, although equally we also recognise that it is an ambitious request given the competing perspectives about what such a “purpose” should be and the competing political ideologies at play—e.g. there are competing views on whether deregulation can help or hinder competitiveness.

67. Delivering an industrial strategy that is able to chart a clear path through tensions and genuinely ensures a coordinated approach to reconciling policy tensions will require a step-change in inter-departmental cooperation (and cooperation with the devolved governments), something which successive administrations have failed to achieve. A whole-of-Government approach was expressed as an ambition of industrial strategy under both the last Labour government and the Coalition Government, but we heard that this was challenging to realise. As the Rt Hon Sir Vince Cable told us, “some bits of Government were very well engaged and very positive […] there were, however, bits of Government that did not engage.”

68. We believe that a better coordinated approach from Government can only be led from the top. The fact that the Prime Minister is chairing the Cabinet Committee on the Economy and Industrial Strategy provides a real opportunity to improve coordination, as does the Secretary of State for Business’s attendance at a significant number of Cabinet Committees. However, many of the pillars outlined in the industrial strategy are discrete responsibilities of particular departments and there is a risk that these are implemented in silos rather than by Government identifying and exploiting potential synergies, trade-offs and linkages.

69. As the Prime Minister’s Chief of Staff, Nick Timothy, has previously commented in the context of Spending Reviews, when allocating resources the Government often makes the assumption that “the baseline for any public spending is broadly right, and

102 Q54 [Rt Hon Sir George Osborne MP]
103 EEF (ISG0067)
104 Q134 [Dr Hamid Mughal]
105 For example, see Institute of Economic Affairs (ISG0045) and New Economics Foundation (ISG0172)
106 QS
officials and Ministers seek to negotiate from there.” A similar risk applies to silo-based industrial strategy, where all Government departments are asked to contribute and simply take a business as usual approach rather than more fundamentally questioning how they can more effectively address underlying economic problems. For example, the Chancellor, in Autumn Statement 2016, talked about addressing “the housing challenge”. In February 2017, less than a month after the Green Paper on Industrial Strategy, the Government published its Housing White Paper, ‘Fixing our broken housing market’ and, with the exception of two cursory references, did not link in with collaboration between Government and the construction industry. This demonstrates how industrial strategy does not appear to be a priority for other Whitehall Departments.

70. A number of submissions to our inquiry set out the opportunity for industrial strategy to help the UK adapt to growing automation and digitalisation—the “fourth industrial revolution”. While the Green Paper proposes a “review of industrial digitalisation”, potential science and innovation funding for automation, and investment in STEM skills, all of which are welcome, there is little sense of how Government will work together to ensure these efforts are aligned and work together coherently. We take seriously the advice of the former Chancellor of the Exchequer that in order to make industrial strategy something which all departments across Whitehall engage in then “you do need to drive it from the centre.”

71. We strongly support the Prime Minister’s leadership in chairing the Cabinet Committee on the Economy and Industrial Strategy. It is also a positive indication of intent that the Secretary of State for Business, Energy and Industrial Strategy sits on more Cabinet Committees than any other Cabinet Minister, creating scope for a significant degree of coordination. However, we are conscious that ‘joined-up Government’ has remained an aspiration for many years that too often is unrealised in practice. The recent publication of the new Housing White Paper is a disappointing and early illustration that Whitehall does not appear to be joined up when it comes to industrial strategy.

72. We do not under-estimate the challenge of developing genuine cross-Government framework that can identify and exploit synergies between departmental activities to create fresh policy options and bring greater coherence to policy making, but Government needs to clearly articulate how it intends to address it. We recommend that the Government consider establishing a joint unit bringing together civil servants from BEIS, the Treasury, the Department for Communities and Local Government, and the Department for Education to provide an inter-departmental team to develop and implement the industrial strategy.

**Designing strategic interventions**

73. As the Institute for Government noted, a “strategy needs to be more than a drawing together of good but unconnected policies though: it needs to be built around a clear

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108 For example, SEMTA ([ISG0026](#)) and General Electric ([ISG0108](#))
109 Q54
mission”. The current Secretary of State for Business suggested in evidence to us that even without the additional hurdle of coalition, Government often faces a challenge in being genuinely strategic and that “the word ‘strategy’ tends to be applied pretty liberally to documents and policies in Whitehall.”

This challenge is borne out by our own analysis of the Productivity Plan, which in our view presented a large basket of disparate policies rather than a considered deployment of specific, strategic interventions. We do not expect Government to shackle every policy to its industrial strategy and nor should Government loosely ascribe the term industrial strategy to any announcement it makes that relates to economic or social policy. As the academic Richard Rumelt has written: “The brilliance of good organization is not in making sure that everything is connected to everything else […] Good strategy and good organization lie in specializing on the right activities and imposing only the essential amount of coordination.”

74. The Industrial Strategy Green Paper does contain a significant number of new commitments (64 out of a total of 106 listed actions), but the remainder are reiterations of previous policy announcements. Furthermore, a number of the new commitments are simply next steps in implementing previous policies or promises to produce more strategies and roadmaps, and several relate to specific investment proposals rather than setting out how future decisions will be guided. This is not necessarily a bad thing: there will never be a ‘Year Zero’ for government, even for a new administration. However, it leaves little if anything that gives a sense of how Government will determine which sectoral “deals” will be prioritised, how decisions on future investment could take into account regional productivity imbalances, or how the Government will determine whether its marginal pound is best spent on improving skills or boosting exports.

75. While clarity on existing commitments is undoubtedly welcome, it sits oddly with us that pre-existing policies have been shoehorned into a new strategy, rather than the strategy setting out design principles that new policies follow on from. We regret that after being seven months in development, the Green Paper does not articulate a more detailed framework for how future decisions will be made. Given that the Government’s recent response to our Report on the Productivity Plan indicates that Plan is still continuing to be implemented, it is also unclear what the relationship between the Productivity Plan and the industrial strategy will be, especially given that the Green Paper makes no mention of the Plan whatsoever. This does not fill us with confidence regarding the Government’s ability to develop coordinated and coherent thinking.

76. Industrial strategy needs to provide a clear framework for how government will make policy choices. Trade-offs will need to be made between where Government spends its marginal pound—for instance, whether that is better invested in skills or in science and innovation or whether it is better invested in London or Leeds. We do not believe that the approach adopted in the Productivity Plan, which was essentially a wide-ranging assortment of loosely connected policies, many of which were pre-existing, is a good model to follow.

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110 Institute for Government, Seven ways for the industrial strategy to succeed, 23 January 2017
111 Q103
**Industrial strategy and Brexit**

77. Another area where further clarity is needed is on the relationship between the Government’s industrial strategy and its negotiating priorities for leaving the European Union. As Lord Mandelson told us, “Brexit is the elephant in the room in all our discussions about industrial strategy.”  

113 A number of submissions to our inquiry both highlighted the opportunities and challenges posed, most frequently in relation to concerns over the future of free movement.  

114 Some commentators have also suggested that negotiations over trade deals could pose challenges for domestic economic and social priorities.

78. The recent White Paper on the UK’s “exit from and new partnership with the European Union” contains only five references to the new industrial strategy, all of which are in the section relating to science and innovation.  

116 All of the references relate to existing domestic commitments made in the Industrial Strategy Green Paper. The only clarity given on the future relationship with the EU on science and innovation is that “we would welcome agreement to continue to collaborate with our European partners on major science, research and technology initiatives.”

117 The Brexit White Paper refers to “five broad sectors covering the breadth of the UK economy; goods; agriculture, food and fisheries; services; financial services; and energy, transport and communication networks.”

79. The Government needs to clarify the relationship between its industrial strategy and its strategy for negotiating the UK’s future relationship with the EU. It is unfortunate that the recent White Paper on exiting the EU fails to do this in any meaningful way and reinforces a lack of coordination between the Government’s major challenge and its principal plank of business policy. It is logical for negotiating positions to be shaped and informed by the UK’s industrial strategy.

**Building support for a long-term strategy**

80. Much of the evidence to our inquiry emphasised the need for Government to work in partnership with business, local government, academia, trade unions and communities in order to develop and deliver its industrial strategy. We fully agree with and support the Secretary of State’s sentiment that it “cannot be a strategy that is simply written behind closed doors.”

119 An industrial strategy, in the words of one witness, “is not about doing unto but doing with” industry.  

120 This is not the same as opening the door to special pleading; proper engagement must involve making conscious efforts to avoid group-think by seeking out diverse views and opinions.

81. It is only through broad and deep collaboration, not only with business but also with trade unions, academics and all interested stakeholders, that the Government can build the lasting support necessary to deliver the long-term industrial strategy that business,
Government, and this Committee aspire to see. As the Secretary of State acknowledges, a key test of industrial strategy is the extent to which it “commands the support and the participation of all sectors of the economy, industries” that will enable it to endure.\textsuperscript{121} We would stress that this cannot only involve business representatives but also needs to build support from trade unions and other economic actors. If industrial strategy is to be a success, it needs to have institutional and cultural pillars which command support and buy-in from relevant groups and which can survive the end of any particular government. Whilst we do not advocate a revival of the corporatist ‘Neddy’, institutions such as the Automotive Council and the Aerospace Growth Partnership demonstrate how industry-Government collaborations can transcend parliaments and provide long-term policy stability for such industries.

82. \textbf{It is clear that for a strategy to be genuinely long-term, Government will need to build a strong coalition of support for its objectives across economic actors. Failure to do so will critically undermine aspirations for a strategy which lasts longer than a single minister or Parliament.}

\textit{The challenge of adversarial relationships}

83. As part of our inquiry we visited Sweden to learn about the implementation of industrial strategy there. We were struck by the consensus within business, government and unions that the role of industrial strategy is “to protect the sailors not the ship”. Essentially industrial strategy’s purpose was seen as ensuring that people of working age had the support they needed to thrive in the workplace and protection during times of unemployment, while recognising that it was in no-one’s interest to protect jobs at the expense of productivity. Within the UK we heard frank and positive evidence of constructive, collaborative working relationships between business and unions. We heard the CEO of Aston Martin tell us how “unions and manufacturers have a common goal, which is all about longevity of industry in this country and in this region and basically keeping long-term employment.”\textsuperscript{122} The representative from Unite the Union told us about the progress in industrial relations in the car industry in recent decades.

“\textquote{There has been trust built up, I believe, in many instances. That does not mean to say that everything in the garden is rosy but the reality is that there is an element of trust and consultation. If you talk to anybody who was in the car industry 30 or 40 years ago, they will say that basically the unions and the employees sometimes deserved each other. That has been said by employers as well.”}\textsuperscript{123}

Unfortunately, we can all readily call to mind recent examples where relationships between business and unions do not demonstrate this level of maturity. Likewise, at a political level, robust debate and challenge between political parties is a healthy part of the democratic process, but when political short-termism leads to frequent and disruptive policy changes announced for the sake of expediency then it undermines the effectiveness of Government. As the former Business Secretary, the Rt Hon Sir Vince Cable told us, “Whenever you get new politicians in post, they always want to announce new things. The

\textsuperscript{121} Q85, Work of the Department 2016–17, 14 December 2016.
\textsuperscript{122} Q197 [Dr Andy Palmer]
\textsuperscript{123} Q198 [Tony Burke]
key thing is the continuity that has underlined the approach.” A genuinely long-term strategy will require a balanced policy approach that looks to build wide consensus, focuses on evidence-based policy, and avoids being prone to instability caused by ideologically driven investments or regulatory changes that are unlikely to outlast the political cycle.

84. An adversarial culture, not just in parliamentary politics but in industrial relations, inhibits the possibility of a successful long-term industrial strategy. It is notable that those sectors which have seen success in recent years, particularly aerospace and automotive, have very productive and positive relationships between management and unions. It is crucial that the Government’s industrial strategy sets out strong mechanisms for dialogue and collaboration with businesses (of all sizes) and unions, aimed at facilitating consensual agreement on future policy direction where appropriate. In responding to this Report, the Government should articulate how it plans to establish long-term stability within its industrial strategy.

**Engaging across industry**

85. With the Government calling on sectors to propose deals, there is a risk that some businesses and sectors, and particularly SMEs and entrepreneurs, are left out in the cold because they are less well equipped to influence Government policy. While supporting a sectoral approach overall, the EEF, for instance, recognised that its implementation under the Coalition Government was not without its challenges: “While economic analysis was produced to support the initial sector choices, the criteria for selection was not seen as sufficiently transparent and some cross cutting technologies and capabilities fell outside the scope of the sector councils.”

86. Although inviting businesses to develop proposals, ‘bottom-up’ as opposed to defining sectors ‘top-down’ should help mitigate this problem, Government only has a finite amount of time and resource and inevitably it will focus more of its efforts on supporting some “deals” over others. This could mean that sectors and businesses which are able to lobby effectively get the most attention, even if they may not be the best placed to deliver “an economy that works for everyone.” As one submission to our inquiry explained, “A sectoral approach can risk ignoring many sectors to support only a chosen few, which would not tackle structural weaknesses in the economy.”

87. We agree with the Secretary of State that the industrial strategy must be developed collaboratively with industry but in doing so, the Government must engage widely and not fall prey to group-think or “capture” and must be clear and transparent about the purpose of its engagement. Collaboration must not be based on behind-closed doors deals with specific sectors or groups of sectors that have the strongest lobbying power at the expense of achieving the Government’s long-term economic and social vision. While it is to be expected that some of the UK’s largest employers and most successful companies are able to secure direct access to Ministers, the Government must ensure that industrial strategy does not become a vehicle for acquiescing to special pleading that protects and entrenches incumbents and disregards the need of less established or unified sectors, disrupters, or smaller businesses.
88. The publication of Ministers’ and Permanent Secretaries’ meetings goes some way to providing transparency about lobbying access. However, many decisions and recommendations around policy design and implementation are developed by staff at more junior levels. Furthermore, the lack of a single unified register of meetings makes it hard for members of the public to navigate the data that is published. As set out in the Government’s recently published Digital Transformation Strategy, the internet has the potential to “improve trust between citizens and state” and make government activity “more transparent.” A concrete step that could be taken to deliver this would be to transform access to transparency data to make registers of meetings more accessible and to develop a non-bureaucratic way to publish details of meetings with external stakeholders at all levels of the Senior Civil Service. **We recommend that the Government improve the transparency of its engagement with business by publishing details of external meetings in a single, searchable database and extending publication to include all meetings that take place at Senior Civil Service level.**

89. One of the criticisms of previous industrial strategies is that they have been overly focussed on top tier companies, “assuming that addressing growth and productivity in these key sectors would automatically pull demand through from UK supply chains”. It has been suggested to us that the “low visibility” of much of the UK’s supply chain has led to gaps in understanding of the UK’s potential capabilities. As we heard from the CEO of Aston Martin, Dr Andy Palmer:

“We rely very much on a supply chain that is offshore. Through the hollowing out of industry through the 1980s we have lost that supply chain and we have to try to bring it back because much of the intellectual property that exists in a car does not exist in the OEM itself, it exists within the supplier. If you do not have that industrial strategy and if you cannot protect the supply the OEM has all sorts of other problems, not least currency exposure in the current climate.”

90. Future industrial strategy should consider UK supply-chains as a whole, with a view to ensuring that proposals are developed that reach across industry. This is one of the key reasons why we eschew an explicit sector-based industrial strategy, as it fails to capture a lot of the potential of industry’s supply chain, which will operate in different sectors. Large companies can have a huge influence on their supply-chains and Government needs to work more effectively to utilise and leverage this potential influence to achieve productivity gains throughout the economy. **A weakness of previous strategies is that they have largely engaged with top-tier companies but not engaged deeper into supply-chains. The Government’s industrial strategy needs to actively ensure that any policy interventions reach throughout the supply-chain.**

**Simple, accessible, understandable and relevant**

91. We were concerned by the evidence we heard that previous industrial strategies had “failed” SMEs by focussing support on large sectors and the UK’s biggest businesses.
One way that Government can avoid a disproportionate focus on larger businesses and more unified sectors with greater lobbying power is to consciously build consideration of SMEs into business engagement and deals. We welcome the signs in the Industrial Strategy Green Paper that the Government is conscious of this. However, as with many of the themes of the industrial strategy, effectively supporting and engaging with SMEs has been a long-running aspiration for successive governments, but it is unclear how substantial progress has been. It is telling that even some of the UK’s largest companies have explained how it is challenging to engage with Government on business policy:

“The ambition to improve policy-making, responsiveness and economic growth through new structures is a valid approach and positive ambition. However, it can be a challenging and often confusing landscape, requiring significant resource and time to be able to shape and benefit from outputs. We have limited resources and time to attend more meetings, support activities, events and groups, including locally. In an increasingly competitive sector such as automotive this can present a challenge. There must be a clear commitment to minimising bureaucracy and complexity.”

While devolution deals and the renewed focus on place has been welcomed by many respondents to our inquiry, and do provide the opportunity for local areas to ensure that their business communities are not neglected, there have also been concerns expressed that these could lead to “a complex landscape for business to navigate, especially with the inherently asymmetric nature of devolution which is developing differently across the UK.”

92. Structural complexity aside, the volume of Government policies can be a challenge for business to understand, even where those policies are designed to offer support. For instance, the GOV.UK website section on “Finance and support for your business” lists 511 available schemes. Even though Government does provide some tools to search through for the most relevant schemes, the volume of schemes to investigate alone creates a significant task for time-poor SMEs. Due to the way that funding programmes often have to meet narrowly defined criteria, even local schemes can be both niche and multitudinous, for example Worcestershire alone offers 22 different business support schemes.

93. In developing its industrial strategy Government needs to pay greater attention to the customer journey for businesses looking to access advice and support. Currently, there is a confusing and complex landscape of policies and interventions designed to support businesses. This has been a long-standing feature of business support from successive well-meaning but ultimately counter-productive actions of successive governments. This approach may benefit from a clear and consistently promoted single point of contact to actively help and support businesses in navigating the support available to them—whether that be at a national level or via regional growth hubs. One of the tests of the success of industrial strategy is whether it is readily understandable, relevant and accessible to SMEs. We recommend that the Government work with industry and local government to conduct a holistic review of the business services and support it offers with a view to simplifying access to advice on these in order to improve the ‘customer journey’.

132 General Motors (PEG046)
133 SMMT (PEG047)
135 http://www.business-central.co.uk/funding-finder/ accessed 23 January 2017
Pragmatic support, not palliative care

94. It has been said that “Strategy is a system of expedients […] the development of an original leading thought in accordance with the ever-changing circumstances.” Ministers inevitably need to respond to changing circumstances, external events and sudden shocks and, despite any amount of good planning, there will always be some ‘unknown unknowns’. Whether it be responding to a crisis in a particular industry or providing the assurances necessary to a leading employer to give them confidence to invest, Ministers will have to make difficult and pragmatic decisions on a regular basis. The key ask from a number of those who submitted evidence to us though is that decisions are made transparently in a way which demonstrates a level playing field. BT’s first principle for developing a successful industrial strategy was that it be “evidence-based, with decisions predicated on open and transparent fact-base and modelling assumptions.” One of the reasons why the term industrial strategy had—and continues to have for some—such negative connotations is the examples of the 1970s, when successive governments spent millions of pounds of taxpayers’ money trying to prop up failing industries. This should not be the approach of an industrial strategy for the 21st century, as the Government seems to recognise.

95. The Government needs to retain the flexibility to engage with businesses individually to encourage and support investment in the UK. For instance, we firmly welcome the fact that the Government was able to provide Nissan with assurances that have helped ensure support for tens of thousands of jobs. But such support should be transparent and made within a clear and understandable policy framework.

96. As has been the case with its efforts to support the steel industry, the Government should support industries it considers to be subject to anti-competitive pressures. But support should be in the context of helping industries that are facing challenging economic situations to adapt and thrive sustainably. Industrial strategy must not provide palliative care for failing and obsolete industries. Where industries are unsustainable, the Government’s priority should be to support individual workers, not to prop up particular companies.
4  Horizontal policy pillars

97. This Chapter considers the horizontal policies outlined as part of the Government’s proposed industrial strategy. Given the time constraints on our inquiry and our own resource limitations as a Committee we have not scrutinised each of the commitments or policy pillars in detail. However, we do have a number of reflections and recommendations based upon the evidence we heard.

Science and innovation

98. Many witnesses to our inquiry highlighted a successful innovation ecosystem as key to boosting productivity. In addition to the challenges discussed in Chapter 2 of this Report, a number of particular themes emerged in evidence, including around the implications of leaving the EU on access to research, the importance of enabling and supporting disrupters, and the most effective ways to use public funding to leverage private sector investment. In the course of our inquiry we also visited two catapult centres, and saw first-hand the work that can happen when academia, the public sector and the private sector come together to boost commercialisation of cutting-edge innovation. As the Director of Global Manufacturing at Rolls-Royce told us, “The High-Value Manufacturing Catapults have plugged a massive gap that we used to have for decades and for me, honestly, if we had Catapult centres 20 or 30 years ago, we would not have some of the issues that we now face in industry.” We also took evidence from representatives of Durham University, Coventry University and University College London, and heard about how university collaboration with business is evolving into stronger partnerships that better enable commercialisation of research:

“By working together we are able to open up that underpinning fundamental research that is missing for those organisations. That allows them to take it forward and incorporate it into their products and services, whether that is consumer psychology or a functional service for a polymer or antibacterial work on antimicrobials.”

99. Government has a unique role in crowding in investment into innovation and helping mitigate risks to business. We agree with the Secretary of State’s assessment that the UK needs to do more to commercialise its world-class R&D base and welcome commitments to do so. Catapult Centres are a promising model for public-private collaboration and we urge Government to allow them time to grow and avoid unnecessary tinkering. We also welcome evidence that universities are increasing their focus on commercialising their research; this should continue to be encouraged and supported.

100. Although, as set out above, we do not think the Government should set arbitrary targets, we do think there remains a strong case for a clear signal that the UK should be working towards ensuring 3 per cent of GDP is invested in R&D. We called for this

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138 E.g. ISG133, CBI which stated that one of the principles of the industrial strategy should be a “willingness to back innovation and be bold at scale”
139 Russell Group (ISG071)
140 Institute of Directors (ISG025)
141 SPRU (ISG111)
142 Q113
143 Q368 [Dr Thompson]
originally in our Report into the Government’s Productivity Plan,\textsuperscript{144} in order to ensure that we catch-up and keep pace with our economic competitors. As we heard, it is important to achieve the “international gold-standard” of 3 per cent “to keep the UK ahead of the curve in tech, engineering and science.”\textsuperscript{145}

101. Clear targets can give focus and energy to the direction of Government policy. While the Government’s commitment to an additional £2 billion of funding for science and innovation is welcome, we reiterate our call on the Government to formally set a target of increasing public and private R&D investment to 3 per cent of GDP.

102. \textbf{We are disappointed that the Government’s response to our Report on the Productivity Plan did not accept our recommendation to set a target of increasing public and private R&D investment to 3 per cent of GDP.}

103. \textit{We repeat our previous recommendation that the Government should set a target to increase R&D investment to 3 per cent of GDP and implement policies to achieve it.}

\textbf{The tax environment for R&D}

104. We welcome the fact that the Government has launched a review of the tax environment for R&D. While HMRC has concluded that R&D tax credits, for instance, provide value for money,\textsuperscript{146} some academics have expressed doubt about their effectiveness, noting that UK investment in R&D as a proportion of GDP has continued to decline despite their introduction and arguing that more direct funding such as the Government’s Small Business Research Initiative (SBRI) may be more effective.\textsuperscript{147} Likewise, it has been argued that initiatives such as the Government’s Patent Box programme may be more likely to impact on multinational corporations’ tax planning arrangements rather than on the location of R&D.\textsuperscript{148}

105. Any radical changes to the R&D tax credit policy would run counter-productive to the need to give businesses certainty and stability to invest, particularly under current circumstances. We therefore think that scrapping these policies would send the wrong signal, but Government should not shy away from strong measures to ensure additionality.

106. \textbf{As part of its review of the tax environment for R&D, the Government should not shy away from ambitious measures to ensure additionality.} These could potentially include: requiring reinvestment of tax saved in R&D, requiring year on year increases in R&D budgets, and/or a tapered rate with greater tax relief on larger investments proportionate to company size/turnover. These are suggested areas for exploration rather than specific policy recommendations. We recognise that each of these options would need considering in more detail to identify and address any risks of unintended consequences.

\textsuperscript{144} BIS Committee, Second Report of Session 2015–16, \textit{The Government’s Productivity Plan}

\textsuperscript{145} ICAEW (SSG0183)

\textsuperscript{146} HMRC, \textit{Evaluation of Research and Development Tax Credit}, March 2015

\textsuperscript{147} For example see David Connell, \textit{Creating markets for things that don’t exist}, Centre for Business Research, University of Cambridge (November 2014)

\textsuperscript{148} As above.


**Embracing disruption**

107. In his foreword to the Industrial Strategy Green Paper, the Secretary of State writes of the importance of making the UK a fertile ground for new industries "which will challenge and in some cases displace the companies and industries of today."\(^{149}\) We wholeheartedly embrace this openness to innovation and disruption. Disruptive technologies and business models by their nature are hard to predict and it is crucial that we do not support incumbents without recognising the inevitability and importance of change. As one witness pointed out, “If you look at the technology roadmaps that were written in the 1980s and the beginning of the 1990s, none of them saw the internet coming.”\(^{150}\)

108. The UK has been seen as a positive climate for disruptive companies and technologies to develop in, and the Government has been described as a “vocal champion for new and disruptive technologies over the past six years.”\(^{151}\) We heard that our openness and our world-class science and engineering base have given us a comparative advantage for innovators and disruptors.\(^{152}\) A hands-off regulatory approach has been seen as a benefit for disruptive business models.\(^{153}\) However, we have also heard that new businesses can exist in “a twilight zone of regulatory uncertainty” that can pose “potential existential threats.”\(^{154}\)

109. Models such as the “regulatory sandbox” introduced by the Financial Conduct Authority were seen as a positive and pragmatic response to encouraging growth in a nascent sector.\(^{155}\) Although we did not hear a significant volume of evidence on this issue, the “sandbox” approach appears to have merit and lessons may be usefully applied to other sectors of the economy. One witness suggested that it could be implemented at a local level, facilitating early stage commercial market development “by giving regional governments power to declare geographically limited sectoral innovation zones.”\(^{156}\)

110. We recognise that the Productivity Plan included a commitment for Government departments and regulators to develop “innovation plans” to set out how legislation and enforcement frameworks could adapt to emerging technologies and disruptive business models. But the fact that these were due to be published in Spring 2016 and are now delayed until “early 2017” does not give us confidence in the ability of Government to keep up with the rapid pace at which disruptive technologies can emerge and develop.

111. While recognising that regulatory landscapes may need to evolve rapidly, giving short-term clarity of regulatory approaches to new industry models and commitments not to retrospectively impose penalties on the basis of initial advice could help give businesses greater confidence to innovate. *In line with the Secretary of State’s stated aim to support disruptors and economic innovation, we recommend that the Government review with industry whether additional steps are needed to provide regulatory certainty for emerging business models.*

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150  Q113 [Professor David Greenwood]
151  IOD (ISG025)
152  Centre for Process Innovation (ISG033)
153  IOD (ISG025)
154  Q345 [Mark Littlewood]
155  Responsible Finance (ISG062)
156  Matthew Rhodes (ISG069)
Skills

112. Throughout our inquiry we have heard that addressing the UK’s skills base is perhaps the most important factor underpinning a successful industrial strategy. Ed Twiddy, Chief Innovation Office at Atom Bank, and formerly a senior official in both local and central government, said that skills “is truly everything”, and Lord Heseltine told us in no uncertain terms that, “if I could design an industrial strategy, it would start in the primary schools.” However, unless Government funding is reprioritised, the scope to introduce new initiatives to support delivery of industrial strategy in schools will be highly constrained by the fact that mainstream schools in England are expected to make £3 billion of efficiency savings by 2019–20, at a time of rising pupil numbers—effectively, meaning an 8 per cent real-terms reduction in funding per pupil.

113. The Industrial Strategy Green Paper makes a commitment to introducing a “proper system of technical education”. This is something we called for in our inquiry into the Productivity Plan, where we emphasised the need for parity of esteem between vocational and academic training. That said, we note that the announcement of £170 million funding for new ‘Institutes of Technology’ is considerably less than the £240 million allocated for Grammar schools expansion in the Autumn Statement 2016. Furthermore, while the funding commitment is new, the policy proposal for Institutes of Technology was actually announced in the Productivity Plan, and the proposals to simplify and streamline the number of qualifications in professional and technical education are also key elements of the Productivity Plan. A “new commitment” to “explore and further encourage the uptake of STEM subjects” is also vague and suggests little by way of a change in direction, as we assume that Government would already have been doing this in light of the emphasis successive Ministers have placed on the importance of STEM.

114. Many of the specific measures announced relate to school-age education. While a commitment to “explore ambitious new approaches to encouraging lifelong learning” is welcome, it is a shame that the more specific proposals on adult learning were not developed to inform discussions around the Green Paper. This is a significant omission given the OECD’s estimate that 9 million working-age adults in England have low literacy and/or numeracy skills. In the context of increasing automation and digitalisation of manufacturing and services, our education system needs to be nimble and able to adapt to future skills requirements. A significantly greater emphasis on whole-life reskilling will be essential to support people to stay in or gain meaningful and high productivity employment.

115. A skilled workforce is an essential foundation of economic success. Given the weaknesses identified by the Government in the UK’s skills base, the proposals contained in the industrial strategy Green Paper leave much to be desired. After six months in development we expected more than a disappointing combination of re-announcements, continuations of existing policy, and vague aspirations. It is

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157 Q379
158 Q64
159 National Audit Office, Financial sustainability of schools (December 2016)
162 Although media reports announced an extra £200 million for Grammar Schools, the detailed tables in Autumn Statement 2016 indicate that has allocated £60 million a year for four years.
deeply disappointing that the Green Paper fails to outline any detailed proposals for discussion in relation to encouraging the uptake of STEM subjects, and improving the skills of those already of working age. These will need to be addressed far more comprehensively in the White Paper. We welcome commitment to a proper system of technical education, linked to local needs, but it is unclear how this actually goes beyond proposals contained in the previous Productivity Plan. The Government needs to set out more detail about how it will achieve parity of esteem between vocational and academic training in practice.

Setting skills priorities at a local level

116. A number of submissions to our inquiry particularly highlighted the importance of “place” in relation to setting priorities for skills. Although the Green Paper states that it will “take further actions to address differences in skill levels between different areas”, it is unclear how the Government intends to work in partnership with Local Enterprise Partnerships (LEPs) and local authorities to achieve this aim. We heard from one witness that “the current fragmented system can lead to perverse outcomes in post-16 skills, for example with people training for roles in which there are either no jobs, or where supply already outstrips demand, whilst other roles remain vacant”, and that devolution of the 16+ education system could better enable skills support to be linked to local priorities. While proposals for devolving employment and skills are welcome, we also heard frustration that the benefits of this “remain constrained by limitations and caveats set by national government.”

117. We recommend that the Government consider the potential for greater devolution of responsibility and funding for skills to local authorities and Local Enterprise Partnerships, who are well placed to work to identify regional needs and design appropriate solutions.

Skills and freedom of movement

118. Evidence from a range of sectors expressed concern about the impact of proposals to curtail freedom of movement on the UK’s future economic success. We heard, for instance, that freedom of movement underpins a successful service based economy, that curtailing freedom of movement could have a significant impact on infrastructure and housebuilding projects, and that freedom of movement is important to the success of our universities. This is a clear example of an area in which the Government’s industrial strategy needs to underpin its approach to Brexit negotiations and future immigration policy.

119. It is also unfortunate that the Government apparently has not previously sought to develop an “authoritative view of the sector specific skills gaps that the UK faces”, particularly in the context of plans to curtail freedom of movement. We question what Home Office “shortage occupation list” for work permits was based on to-date.

164 HM Government, Building our Industrial Strategy: Green Paper, p.48
165 Core Cities (ISG186)
166 Newcastle City Council (PEG049)
167 ICAEW (ISG0183)
168 TUC (ISG112)
169 Q248 [Dr Sarah Main, Dr Celia Caulcott]
120. Improving workforce skills is a long-term project and, in the interim, Government will not be helping anyone if we starve our businesses of the talent they need to succeed. Any moves to place further limits on free-movement in the near future need to be carried in the context of a clear plan to ensure that the UK has a solid skills-base to meet industry’s current needs.

121. While for certain low-skilled employment, there may be a case for restrictions on free-movement given that businesses should be able to secure the necessary labour from within the existing UK market, the ability to retain, attract and access skilled workers will be essential to ensuring that we are able to actively attract the best talent to the UK. As a country we need to develop our workforce to be able to compete with the best. **In the context of negotiations over free-movement as part of withdrawal from the EU, the Government must ensure that businesses continue to be able to access the skills they need. In its response to our Report, the Government should provide further clarity on how it intends to do this.**

122. **We recommend that the Government exclude university students from immigration totals and promote high skilled migration to the UK on an equal “who contributes most” basis to people wishing to invest and innovate in the UK.**

**Infrastructure**

123. We heard strong support for inclusion of infrastructure in the Government’s industrial strategy, with evidence placing an emphasis both on the importance of upgrading our physical and digital infrastructure. We also heard evidence of significant disparities in infrastructure spending per head of population around the country, with IPPR North stating that by their estimates this stood at £2,600 per person in London compared to £380 per person in the North for planned transport infrastructure investment.\(^{171}\) That successive Governments have failed to invest sufficiently in infrastructure because the benefits only occur outside of the electoral cycle illustrates the need for an industrial strategy that can provide a framework for long-term investment. While the Green Paper went on to include a number of new commitments to specific infrastructure projects, and we welcome the Government’s commitment to longer-term planning and investment in infrastructure, the Green Paper was unclear about what framework the Government proposed to use to rebalance spending. The Industrial Strategy Green Paper contained a commitment to “use infrastructure to support rebalancing”, and said that, “We will continue to prioritise the highest value-for-money projects, as we seek to address productivity weaknesses across the country.”\(^{172}\) However, there is a potential tension within this proposal in that the highest value for money projects may not always be those which address productivity weaknesses across the country.

124. We assume that to date the Government has already been prioritising “the highest value-for-money projects”, in line with the Treasury Green Book—the document which provides guidance on “ensuring public funds are spent on activities that provide the greatest benefits to society, and that they are spent in the most efficient way”.\(^{173}\) However, it appears that the current approach to investment appraisal and decision-making has led to widespread regional disparities in spend. In this context we heard evidence that

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\(^{171}\) IPPR (PEG007)


Transport for the North are working with the Treasury and the Department for Transport to address the “challenge” of developing new evaluation frameworks that incorporate the potential benefits that transformative infrastructure investment can unleash:

“At the moment it is all demand-led, marginal or incremental change in transport that delivers a certain set of outcomes. We are looking to see what transformation will look like and how that impacts on the tax take or the benefit of expenditure that might be coming out of central government anyway.”174

125. Decarbonising the economy, ensuring we have a functioning transport system, enabling UK businesses to be at the forefront of the digital revolution and improving flood defences, all require decisive, long-term and strategic investment throughout the UK. We welcome the commitment to boost infrastructure investment to 1.7 per cent of GDP over the course of this Parliament.

126. The industrial strategy provides a welcome opportunity to set out a clear framework for making future decisions on infrastructure investment, but balancing boosting overall productivity with supporting growth in the UK’s different nations and regions will inevitably involve trade-offs around where funding is spent. It is unfortunate that the Green Paper does not address this tension openly, nor provide a suitable framework and criteria by which infrastructure will be allocated. We presume that the Government has always prioritised “the highest value-for-money projects”. Given this, we would welcome clarity on how its approach will differ in the future to better support rebalancing.

The role of the National Infrastructure Commission

127. In our Report into the Productivity Plan, we broadly welcomed the creation of the National Infrastructure Commission, noting the importance of its direct accountability to Parliament. Given that the purpose of the creation of the National Infrastructure Commission was to put infrastructure development on a long-term and stable footing, we were therefore surprised that the Government rolled-back from its initial intention to place the Commission on a statutory footing.

128. The decision not to place the National Infrastructure Commission on a statutory footing risks creating the impression that the Government is not backing up its aspiration for a long-term policy framework with action that will help embed that.

129. We are surprised that the National Infrastructure Commission gets little prominence in the industrial strategy and it is unclear how the questions in the Green Paper are intended to complement the Commission’s own call for evidence. For example, has the Commission been asked to prioritise rebalancing in its assessment of the country’s infrastructure requirements? We would welcome clarification from the Government.

Supporting businesses to start and grow

130. We welcome the Government’s focus on supporting businesses to grow and on considering the need to strengthen corporate governance. Both of these are issues we have
taken a close interest in over the past year, including through our inquiry into Access to Finance and our Reports into Working Practices at Sports Direct and, jointly with the Work and Pensions Committee, the collapse of BHS. In September 2016 we launched an inquiry into Corporate Governance, which we hope will contribute to the Government’s own thinking.  

175 We note that there have also been a number of other reviews in recent years into the UK’s poor track-record on scale-up, such as the work by Sherry Coutu CBE.  

176 The problem of impatient capital and the UK’s poor track-record on scale-up have been subject to a number of reviews in recent years. We welcome the fact that Government is taking this issue seriously and look forward to seeing the review followed by meaningful action. We will also continue to consider this issue as part of our inquiry into Corporate Governance and a new inquiry into Scale-Up.

**Improving management skills in business**

132. In our inquiry into the Productivity Plan we heard that weaknesses in the leadership and management skills within industry was undermining our productivity.  

177 We welcome the additional clarity on the steps Government are taking to address this provided in their response to that Report, which included an additional £24 million funding for Growth Hubs. There is, however, a risk that this funding does not achieve its intended benefits. One area of potential concern we have heard is that the Growth Hub network, which provides a gateway and advice service to many businesses seeking support, is providing a “patchy” service and that “there is a need to set a clear national direction and provide stronger support”.  

178 Given the shift towards localised delivery of business support, there is clearly more work to be done in light of research by Institute of Chartered Accountants in England and Wales (ICAEW) which found that “less than half of businesses are aware of LEPs and less than one in five had heard about Growth Hubs.”  

179 Furthermore, the Federation of Small Business told us that they have “consistently raised concerns over a lack of co-ordination and duplication of business support provision across both the public and private sectors, including the interaction between national and local schemes.”

133. Evidence on the impact of Growth Hubs is mixed. In its response to this Report, Government should set out how it intends to evaluate the impact of current funding in order to determine what needs to be done to support Growth Hubs to provide a better service in the future.

**Creating the right incentives for long-term investment**

134. One issue that the Industrial Strategy Green Paper rightly considers is the fact that the United Kingdom has lower levels of fixed capital investment than competitors in other countries. One of the key tools that has been used by Government to encourage business investment in recent years has been adjusting the corporation tax rate. HM Treasury has written that one of the reasons for having the lowest corporation tax rate
in the G20 is to “increase the investment and productivity that drive economic growth.”\textsuperscript{181} Government’s own modelling of corporation tax cut reductions implemented in the 2010–15 parliament suggested that they would increase: business investment, GDP, demand for labour, wages and consumption.\textsuperscript{182} However, we have also heard evidence suggesting that “international data suggests there is little correlation between a country’s corporation tax and its economic performance.”\textsuperscript{183} We recognise that the merits or otherwise of lowering corporation tax are highly politicised issues and subject to considerable debate among different schools of economics. We also note that despite the UK having had some of the most competitive corporate tax rates among comparable economies since the early 1990s our productivity gap has not closed. While the OECD argue that lower corporation taxes can improve productivity, it also notes that trade-offs must be made against other policy objectives, such as improving equality, and that “it is probable that there are diminishing growth returns to adjusting taxes.”\textsuperscript{184}

Figure 7: Corporate tax rates in selected countries, 1981–2015

![Corporate tax rates in selected countries](image)

Source: Institute of Economic Affairs

While we recognise that there are multiple factors which contribute to a country’s productivity, hence the need for a multi-faceted industrial strategy, it would be an omission not to more fully consider the potential role of tax levers in promoting productivity beyond potentially blunt reductions in corporate tax rates. Instead, a more holistic review of the business tax landscape and the incentives it provides to boost productivity is worth further consideration.

\textsuperscript{181} HM Treasury and HM Revenue & Customs, \textit{Analysis of the dynamic effects of corporation tax reductions} (December 2013)

\textsuperscript{182} As above.

\textsuperscript{183} New Economics Foundation (ISG172)

136. Fiscal levers can play a key role in shaping business behaviour. We recommend that Government commission an independent review bringing together broad representation to consider whether taxation levers can better be used to boost investment in physical and human capital, research and innovation.

Business rates

137. With regards to business taxation we also heard that the current business rates system can “penalise” manufacturers for investing in new plant and machinery, creating a perverse incentive against investment.185 While we recognise that the Government’s move to give control for business rates to local authorities is intended to provide “a direct incentive on councillors to allow developments to take place,”186 we are concerned that this will not address the fundamental issue that investing in improving a premises or plant may increase the overall rateable value of the property. It has also been suggested that there is a risk that the move to full business rates retention by local authorities could entrench economic inequalities,187 leaving councils in more affluent areas able to reduce rates further, with councils in deprived areas facing stark choices about whether to cut rates to attempt to attract investment or maintain them to fund crucial local services.

138. We have heard evidence that the current structure of business rates act as a particular disincentive to capital investment and that devolving responsibility for rate setting to local authorities is unlikely to boost investment in those areas which need it most. Furthermore, in an environment where retail is increasingly carried out online, it risks disadvantaging retailers who maintain a physical presence on our highstreets. We recommend that the Government conduct a fundamental review of the outdated structure of the business rates system, given that it acts as a disincentive to investment regardless of who is responsible for setting the overall rate.

Public procurement

139. The UK’s public procurement budget is worth around £200 billion and accounts for around a third of public spending,188 meaning that it can play a significant role in supporting delivery of the industrial strategy. When it comes to public procurement issues, there is clearly a trade-off to be made between reducing short-term costs by maximising competitive pressures through procuring internationally, and delivering long-term value for the UK by investing taxpayers’ money in UK businesses and products where possible. Even within existing EU procurement rules, the Government can procure on ‘Most Economically Advantageous Tender’ principles, which can include criteria such as local economic impact on jobs. For instance, we heard that this approach had been used in the procurement of contractors to deliver the Crossrail scheme.189 However, we have also heard of frustrations where poor procurement planning by Government has led to major contracts going overseas, because successive Governments have not supported domestic

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185 Construction Products Association (ISG024)
186 Q66 [Rt Hon George Osborne MP]
187 Newcastle City Council (PEG49)
188 Unite the Union (ISG048)
189 Rail Delivery Group (ISG017)
industry in a way that enables it to meet current demands.\textsuperscript{190} As the TUC explained, “The
UK has a poor record on the strategic use of procurement to support industrial policy, despite the fact that EU rules allow the creative use of procurement structures.”\textsuperscript{191}

140. We welcome the fact that the Government is considering opportunities to better utilise public procurement to maximise economic opportunity for UK firms, and it should make greater use of flexibility in existing state aid rules prior to our departure from the European Union. The Government should also consider the opportunities to further boost procurement from within the UK as part of its negotiating strategy for withdrawal from the EU.

The Small Business Research Initiative

141. During our inquiry we heard positive evidence in favour of the Government’s Small Business Research Initiative (SBRI) programme. However, we also heard that the US scheme on which the SBRI is modelled was perceived to be far more successful, with the UK scheme too limited in scope by comparison.\textsuperscript{192} In particular, we were told that uptake of the SBRI has been “patchy,”\textsuperscript{193} and its scale is “miniscule” in relation to overall public procurement spend.\textsuperscript{194}

142. We welcome the review of the Small Business Research Initiative that the Government has commissioned; we hope this will be ambitious in its recommendations and that the Government will increase the scale of the scheme and better embed it across Whitehall.

Encouraging trade and inward investment

Supporting UK companies to export

143. We welcome the fact that trade and investment are being considered a core part of the Government’s new industrial strategy. While global growth may partly explain the persistent deficit, it does not explain why UK export growth has been the slowest in the G7 since 2008. As we heard during our own inquiry into Exporting and the role of UKTI, the Government’s previous model for supporting exporting had significant flaws and we welcome the fact that steps are being taken to address these. Responsibility for scrutinising Government exports policy and the work of the Department for International Trade now rests with the International Trade Committee, to whom we wrote to set out the findings from our own work in this area.\textsuperscript{195}

Inward investment

144. Launching her campaign to become Prime Minister, Theresa May spoke of the need to assess foreign takeovers of UK companies to determine whether they are in the national
interest: “A proper industrial strategy wouldn’t automatically stop the sale of British firms to foreign ones, but it should be capable of stepping in to defend a sector that is as important as pharmaceuticals is to Britain.”\textsuperscript{196}

145. Under the current legislation, the Secretary of State for Business may only intervene in takeovers by foreign companies in very specific circumstances. There are presently three public interest considerations specified in the Enterprise Act 2002 as legitimate bases for Ministerial intervention. These are:

- national security;
- media plurality, quality and standards; and
- the stability of the UK financial system.\textsuperscript{197}

146. The UK is a top destination for Foreign Direct Investment (FDI), and in 2015 was reported to be the largest destination for FDI, attracting 28% of total FDI in Europe.\textsuperscript{198}

We have received evidence from a range of businesses in a variety of sectors, expressing concern about what additional Government intervention might mean in practice. Businesses ranging from the glass sector\textsuperscript{199} to the creative industries\textsuperscript{200} were very clear that they had benefited from multinational investment. We also heard that Government intervention could “disincentivise foreign investment”\textsuperscript{201} and could lead to retaliatory behaviour by other countries that would be counterproductive for UK companies.\textsuperscript{202}

However, disadvantages arising from foreign investment were also identified; for instance, that “when corporate decisions are taken, it tends to be the home site that is the last one to be negatively impacted and the first one to see positive investment.”\textsuperscript{203} We heard from Lord Mandelson that he believed it was important to “put some grit in the wheels” of takeovers to ensure they were properly scrutinised; a view shared by Alex Brummer, the City Editor of the \textit{Daily Mail}.\textsuperscript{204}

147. Views on foreign takeovers are highly emotive and potentially distorted by high profile issues such as the Cadbury/Kraft and AstraZeneca/Pfizer takeover proposals. We also note that since the Kraft takeover of Cadbury, and the subsequent reneging on pre-takeover commitments, the Takeover Panel has tightened its rules and that new provisions to ensure post-offer commitments are enforceable are now in place.\textsuperscript{205} These rules are being put to the test for the first time through Softbank’s takeover of ARM, which received significant media coverage in July 2016.\textsuperscript{206}

148. Looking at the data on the volume of inward and outward investments, it appears that patterns of inward and outward investment by the UK are broadly balanced.\textsuperscript{207} The vast majority of inward and outward investment since 2010 has been with the United

\textsuperscript{196} Rt Hon Theresa May MP, \textit{Speech of 11 July 2016}
\textsuperscript{197} Mergers & takeovers: the public interest test, \textit{House of Commons Library, CBP 5374} (September 2016)
\textsuperscript{198} UKTI, \textit{UKTI Inward Investment Report 2014 to 2015}, June 2015
\textsuperscript{199} British Glass (ISG021)
\textsuperscript{200} COBA (ISG167)
\textsuperscript{201} Rolls-Royce (ISG146); MasterCard (ISG044)
\textsuperscript{202} British Aggregates Association (ISG162)
\textsuperscript{203} Q144 [Dr David Greenwood]
\textsuperscript{204} Q353; Q333
\textsuperscript{205} Takeover Panel (ISG020)
\textsuperscript{206} As above.
\textsuperscript{207} Analysis is based solely on the volume of M&A activity, not the value of transactions.
States. The challenge is less about the overall volume of foreign investment in the UK than a judgment as to whether certain industries or sectors should be protected in the national interest. For instance, we heard that while the UK Government has golden shares in BAE Systems, Rolls-Royce and National Air Traffic Services that can be used to prevent foreign takeover, many other countries restrict FDI for a wider range of industries for security reasons.

Figure 8: UK vs. foreign M&A activity

Source: Mergermarket

The UK has been extraordinarily successful in attracting foreign direct investment over the past 20 years. This has improved the business environment, not only through the creation of employment, but by bringing in new ideas and innovations, which have improved the competitiveness and productivity of British business as a whole, with management techniques cascading through the economy.

The UK's openness to foreign direct investment has been an advantage for Britain. The recent deal with Nissan is another example of this, for which the Government should be commended. It is often said that Britain is more prone to “selling off the crown jewels” than other nations. However, certainly when it comes to the last six years, the number of foreign acquisitions in the UK more or less match the number of UK acquisitions overseas. That said, foreign takeovers of major UK national firms, such as Kraft Heinz's recent (and short-lived) proposed takeover of Unilever—the second biggest company by market capitalisation in the FTSE100 and a leading player in food and drink manufacturing, the country’s biggest manufacturing sector—clearly can cause concern. While M&A activity has the potential to improve productivity of an individual company, in the case of an international takeover this risks being at the expense of jobs and investment in the UK unless the Government is able to extract commitments on these. It is not exactly clear the framework or criteria by which the new Government will approach foreign takeovers.

Mergermarket, volume 2010–2016. Acquisitions from the United States in the UK alone were greater than the sum total of the next nine largest overseas investors into the UK by origin country.

TIGA (ISG178)
given the Prime Minister’s rhetoric. **Given the Prime Minister’s previous comments about foreign takeovers, the Government needs to provide much greater clarity and certainty as to what steps it intends to take to intervene in foreign takeover deals and in what circumstances.**

**Protecting taxpayers’ investment**

151. In addition to areas where there are particular national interest reasons to prevent foreign investment, we can also see merit in ensuring that where companies have benefited significantly from taxpayer support then there are restrictions to prevent expertise and intellectual property being developed in the UK from leaving. The former Business Secretary, the Rt Hon Sir Vince Cable, told us that one of his concerns about the AstraZeneca/Pfizer takeover was the “need to have some protection of concentrations of British science, which have been built up over many years with taxpayer support.”

152. **We recommend that the Government takes steps to ensure it has the power to retain IP benefits in the UK in the event of a foreign takeover where a business has been supported in developing new IP through taking advantage of taxpayer funding or tax-incentives. At the very least, it should ensure that any transfer of IP delivers a substantial return for taxpayers. This could be done, for instance, by placing constraints on access to funding and incentives. The Government should also develop mechanisms to clawback any tax relief or funding should tax-payer subsidised IP be transferred abroad.**

**Affordable energy and clean growth**

153. As the Secretary of State has said, the global challenge to decarbonise is not just an imperative on its own grounds but also presents an enormous economic opportunity.

154. Transitioning to a low carbon economy will require significant economic shifts and will affect every sector of the economy. As the Director of Global Manufacturing at Rolls-Royce told us, “industrial strategy is not just meant to fix what is wrong today but to have a longer-term view about how it is that in the low carbon economy […] we will maintain that success for the next 30 to 40 years.”

210 Q38
211 Rt Hon Theresa May MP, *Speech of 11 July 2016*
212 Rt Hon Greg Clark MP, *Speech of 11 November 2016*
214 Aldersgate Group ([SG138](https://www.aldersgategroup.org/))
215 Q112
155. The framework of the “trilemma” exists because it recognises “the need to have a secure, affordable and decarbonised energy supply”\(^{217}\) and that there are inherently trade-offs between policies that deliver this. While security of supply does not have to be delivered through new generation, but can also be delivered through other measures such as smart grids,\(^{218}\) and energy efficiency investment,\(^{219}\) there are trade-offs between the types of approach adopted, the rates of decarbonisation and affordability. Likewise, with regards to meeting future carbon budgets, while clearly we welcome the explicit commitment to this ambition in the industrial strategy, we are deeply worried that the Committee on Climate Change has identified significant gaps between our ambition and our current policy delivery.\(^{220}\) It appears unrealistic to assume that closing this gap can be divorced from issues around the affordability of decarbonisation and the types of energy innovation that the UK should be looking to grow. The fact that progress in reducing emissions since 2012 has been almost entirely due to the power sector\(^{221}\) suggests that the industrial strategy needs to include meaningful policies to support decarbonisation of our industries and buildings. While the Industrial Strategy Green Paper does suggest that the new Industrial Strategy Challenge Fund could support smart and clean energy technologies, and we welcome signs that the Government will establish a new institute to act as a focal point for work on battery technology, energy storage and grid technology, it is important that we also see clear signs as to how Government will embed clean growth in our economic future. For our own part, we continue to see the balance of security of supply, decarbonisation and affordability as equal priorities.

**Figure 9: Progress reducing emissions since 2012 has been almost entirely due to the power sector**

![Progress reducing emissions since 2012 has been almost entirely due to the power sector](source: Committee on Climate Change analysis of DECC data)

\(^{217}\) Renewable UK (ISG171)

\(^{218}\) Institute of Mechanical Engineering (ISG143)

\(^{219}\) New Economics Foundation (ISG172)


\(^{221}\) As above.
While we welcome the industrial strategy’s support for energy innovators, taking advantage of the economic opportunities presented by decarbonisation also means ensuring the UK continues to be seen as a world-leader in the transition to a low-carbon economy. In this context, we trust that the Government will publish its Emissions Reduction Plan by the end of March 2017, as indicated to us by the Minister of State for Climate Change and Industry. The Government needs to ensure that the Emissions Reduction Plan and industrial strategy are coherent and consistent, with commitments in the industrial strategy to actively support delivery of current and future carbon budgets.
5 Rebalancing our economy

157. In recent years, the Government has placed an increasing emphasis on ‘rebalancing’ the UK economy. The July 2015 Budget included references to rebalancing the UK economy geographically and sectorally in order to ensure “a truly national recovery,” and the former Chancellor of the Exchequer also spoke of the need to diversify the UK economy and support a wide range of sectors to grow:

“Yes, we want the City of London to remain the world’s leading centre for financial services, but we should resolve that the rest of the country becomes a world leader in advanced manufacturing, life sciences, creative industries, business services, green energy and so much more. This is our vision for growth. Difficult decisions and major reforms are needed to make it happen, but the alternative is to accept Britain’s economic decline and a continuing fall in living standards for our population, and that is not an alternative anyone in this House should be prepared to accept.”

Geographical rebalancing

158. The Industrial Strategy Green Paper has stated that “A modern industrial strategy will have recognition of the importance of place at its heart.” There are two distinct aspects to this: devolution in England and the relationship between Government in Westminster and the devolved governments in Scotland, Wales and Northern Ireland. The primary focus of our Report is on the devolution relationship in England, as we received very little evidence on the Government’s relationship with the devolved administrations. Furthermore, because many aspects of economic policy are already devolved, much of the Government’s industrial strategy is, essentially, an industrial strategy for England.

Devolution and rebalancing in England

159. The role of “place” in economic policy has increased in significance under the Coalition and Cameron governments. Initiatives such as the Northern Powerhouse and Midlands Engine, together with devolution deals across England, were intended to provide additional powers and funding to boost productivity in those regions. The Productivity Plan included commitments to “rebalancing growth across all regions and nations of the UK.” By April 2016 the Government had agreed ten devolution deals and was considering 34 proposals for deals, which were designed to “respond to broadly-framed objectives to support economic growth and rebalancing, public service reform and improved local accountability”. According to the Local Government Association, devolution deals now cover over 50 per cent of England’s population.

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222 HM Treasury, Summer Budget 2015, 8 July 2015
223 HC Deb, 23 March 2011, Cols 953–4 [Commons Chamber]
224 HM Treasury, Fixing the Foundations, July 2015, p.72
225 National Audit Office, English Devolution Deals, April 2016
226 Local Government Association (ISG016)
160. We heard strong support for the Government’s proposal to increase its focus on place as part of its industrial strategy. As the Local Government Association told us,

“Currently, local leaders across the country can struggle to access the levers of growth and, in turn, match the economic performance of their global competitors. A national industrial strategy which places a strong emphasis on the unique contributions of different places provides a clear opportunity to address this challenge, by significantly boosting the devolution of powers and responsibilities in support of economic growth.”

All three major UK business representative bodies—the Confederation of British Industries, British Chambers of Commerce, and the Federation of Small Businesses—also endorsed a greater focus on place.

161. However, we also heard concerns about whether local institutions have sufficient resources to deliver. A National Audit Office report on Local Enterprise Partnerships found that only 5 per cent agreed that they had sufficient resources to meet the expectations placed on them by Government. These concerns were reiterated to us in evidence from the Institute of Directors. We also heard evidence arguing that “it is likely that a number of LEPs will find that they do not have a level of specialisation sufficient to generate the sort of productivity and employment improvements they are seeking.” Furthermore, concerns were raised about the level of transparency and accountability with which local institutions such as LEPs operate. It was particularly concerning that local authorities also called for the need for greater transparency and accountability in relation to devolution deals. For instance, East Midlands Councils told us that, “if the Midlands Engine is to be a genuine partnership led by LEPs and local authorities, then transparent governance and accountability arrangements need to be put in place.”

162. The Committee welcomes the positive signs that the Government will look to work closely in collaboration with the UK’s various national, local and regional governments in developing its industrial strategy. Where additional powers are devolved, the Government needs to ensure that appropriate funding is also devolved.

163. While variations in perceived performance of Local Enterprise Partnerships are to be expected—that is part and parcel of devolution—the Government has a role in supporting and multiplying best practice. Given the prevalence of concerns and low awareness of LEPs, as well as fiscal constraints, the Government should review LEPs to ensure that needless duplication is avoided, best practice is shared, and value for money is secured. This should include ensuring governance and accountability frameworks are fit for purpose.

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227 As above.
228 Federation of Small Businesses (ISG166)
229 National Audit Office, Local Enterprise Partnerships (March 2016)
230 Institute of Directors (ISG025)
231 Professor Nightingale (ISG134)
232 Federation of Small Businesses (PEG026)
233 East Midlands Councils (PEG030)
The challenge of coordination

164. It is important to also ensure that institutions work effectively together and do not duplicate. One of the concerns we have heard in previous inquiries is the fact that public and professional business bodies can sometimes compete and duplicate activities at a superficial level rather than working together to add value.\(^{234}\)

165. A place based approach can also lead to competition—rather than collaboration—between local areas. Competition in itself is clearly not a negative. But while we heard that regional specialisation, such as clusters, can create “powerful positive benefits”\(^{235}\), we also heard concerns about the abilities of areas to coordinate to deliver these impacts. For instance we heard that “an apparent lack of coordination and information sharing between local authorities, LEPs and business representation \(\ldots\) leads to wasteful duplication of activity in some areas with insufficient attention in others.”\(^{236}\) One concrete example that was cited was the 2003 introduction of a £90 million nanotechnology programme by the then Department for Trade and Industry in 2003; funds were spread too thin, creating 24 centres across the country, many of which struggled to attract sufficient private investment to make them viable.\(^{237}\)

166. The range of different approaches which have evolved as the Government has experimented with greater local devolution have also introduced challenges. Lord Heseltine’s report, _No Stone Unturned in Pursuit of Growth_, cited LEPs, the Growing Places Fund, City Deals, Rural Growth networks, the regional growth fund etc. as positive examples of devolution but concluded that “this approach is piecemeal and creates complexity.”\(^{238}\) We strongly agree with Lord Heseltine in this regard. We have also heard how the “variegated models of decentralisation” create a “daunting challenge” for businesses to navigate,\(^{239}\) and can lead to “multiple or overly bureaucratic systems.”\(^{240}\) As the Society for Motor Manufacturers and Traders told us:

“Devolution deals and new initiatives such as the Northern Powerhouse and Midlands Engine are still developing and the full impact and opportunity for business is yet to emerge. What is clear, however, is that there will be a complex landscape for business to navigate, especially with the inherently asymmetric nature of devolution which is developing differently across the UK.”\(^{241}\)

167. It is likely that there will be tensions between national and regional priorities within England and between Westminster and the devolved administrations. The Government needs to provide clarity on the respective roles and responsibilities between national, local and regional institutions. Failure to do so will lead to unnecessary complexity and confusion for business and reduce accountability to the electorate. In partnership with business representatives, local government and the devolved administrations, the Government should consider whether any further steps are desirable to facilitate

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\(^{234}\) Giving evidence to our inquiry into Exports and the Role of UKTI, Dr Catherine Raines, then Chief Executive of UKTI (now part of the Department for International Trade) said that “there absolutely has been overlap” (Q276)

\(^{235}\) Royal Academy of Engineering (ISG143)

\(^{236}\) UK Metals Forum (ISG035)

\(^{237}\) SPERI (ISG057)

\(^{238}\) The Rt Hon Lord Heseltine of Thenford CH, _No Stone Unturned in Pursuit of Growth_ (October 2012), pp.34–36

\(^{239}\) CURDS (PEG010)

\(^{240}\) Alstom (PEG032)

\(^{241}\) SMMT (PEG047)
businesses in understanding and navigating different tiers of devolution. While many services may best be designed at a local level, the Government needs to ensure that it avoids creating barriers to cooperation between local institutions or inadvertently introducing perverse incentives that lead to needless and inefficient duplication of services.

**Understanding the causes of unbalanced investment**

168. As the industrial strategy recognises, Government spending is a key lever for driving economic outcomes across the UK but, historically, public spending has been skewed towards London and the South East, which have the highest per person funding on research and infrastructure. Analysis by IPPR North has also found that northern secondary schools are, on average, funded £1,300 less per pupil compared to those in London, and northern primary schools are funded £900 less than their counterparts in the capital.\(^242\) While the funding differentials can partly be explained by factors such as the cost of land and labour in different parts of the country, there is a risk that such skewed spending distorts economic growth and the ability to attract and retain a skilled workforce.

169. As the Government looks to rebalance spending, it first needs to understand why disparities in spending between different parts of the UK stand as they are, and to investigate whether any factors of its policy process and modelling for investment decisions have contributed to these disparities.

170. *We recommend that the Government set out a clear plan to close per head spending gap on infrastructure, R\&D and education between London and the rest of England.*

**Devolution and fiscal policy**

171. We note that while many of the policy levers are devolved, fiscal policy remains highly centralised within HM Treasury. For instance, currently around 87 per cent of Scotland’s budget is funded from tax revenues controlled by the UK Government, although further devolution following the Smith Commission will devolve over 50 per cent of this to Scotland from April 2017.\(^243\) In Northern Ireland, devolution of corporation tax has been seen as a significant lever to improve competitiveness with Ireland, and the Northern Ireland Assembly has signalled that it intends to reduce its corporation tax rate to 12.5 per cent from April 2018.\(^244\) As we heard from the Institute of Economic Affairs, “we are still the most centralised state in the Western world with regards to where tax and spending power lies: overwhelmingly in Whitehall,” and it was suggested that fiscal levers could be deployed “sensibly” if controlled at a local level.\(^245\)

172. *While the Government is experimenting more with fiscal devolution, such as the planned devolution of powers to set business rates, it is notable that the Industrial Strategy Green Paper is broadly silent on the potential for further fiscal devolution.*

\(^{242}\) IPPR North, *'Secondary school set back' could cost the northern economy £29bn in lost productivity*, May 2016  
\(^{243}\) Institute for Fiscal Studies, *The Smith Commission’s Proposals* (December 2014)  
\(^{244}\) HMRC, *Northern Ireland Corporation Tax Regime* (September 2016)  
\(^{245}\) Q327 [Mark Littlewood]
Industrial Strategy: First Review

Broadening our economic base

173. The UK has a world-leading services sector and is the second largest exporter of services in the world; however, we also have many low productivity services jobs. Research by the IPPR has indicated that low wage sectors are also frequently low productivity sectors.\textsuperscript{246} Retail, accommodation, food and administrative services employ a third of all workers, produce 23 per cent of the UK’s gross value added, and are on average 29 per cent less productive than the economy as a whole.\textsuperscript{247}

174. It has been argued that it is inherently easier to raise productivity in the manufacturing sector than in the services sector, for instance through mechanization and process improvements, whereas increases in service sector productivity are more readily realised by lowering the quality of the service or, as in the case of the financial crisis, debasing products through excessive risk taking.\textsuperscript{248} While in other rich countries such as Germany and France, the fall in manufacturing as a share of GDP over the last two decades appears quite large in current prices (20 per cent and 40 per cent respectively), measured in constant prices the fall has been less than 10 per cent and, in constant prices, it has actually risen in the United States and Switzerland.\textsuperscript{249} While the UK is the ninth largest manufacturing exporter in the world, we are only 24th in the world in per capita terms, behind both Iceland and Finland.\textsuperscript{250}

175. The Government Office for Science has found that remuneration in UK manufacturing was 10 per cent higher in comparable occupations compared with the average across all industries,\textsuperscript{251} and we have heard from the EEF that manufacturers invest more in R&D and plant than their output share of the economy.\textsuperscript{252} The Office of National Statistics has indicated that manufacturing productivity has grown by 2.8 per cent on average per year since 1948—compared with 1.5 per cent in the services industry—and that labour productivity in manufacturing sector was over twice as high as in services in 2014.\textsuperscript{253} We were also told by Rolls-Royce that manufacturing carries significant “social capital.”\textsuperscript{254}

176. Economies such as Sweden, Germany and Switzerland demonstrate that there is no intrinsic reason for advanced, developed countries to suffer such weak manufacturing performance. Success of automotive and aerospace sectors has been aided by strong Government support and collaboration. But that same level of support has not been consistent more widely across the UK-manufacturing base, as evidenced by closure of the Manufacturing Advisory Service and AMSCI in recent years.

177. While recognising the importance of the services sector, and the UK’s comparative economic advantage, supporting industries which produce goods, technology, and innovation will help boost productivity and create high-quality jobs. We welcome signs that the Government recognises the value of rebalancing our economy in this way.

\textsuperscript{246} IPPR, \textit{Boosting Britain’s low-wage sectors: A strategy for productivity, innovation and growth}, May 2016
\textsuperscript{247} As above; also see TUC (ISG112)
\textsuperscript{249} As above, pp.265–6.
\textsuperscript{251} Government Office for Science, \textit{The Future of Manufacturing} (2013)
\textsuperscript{252} EEF (PEG016)
\textsuperscript{253} ONS, \textit{The Changing Shape of UK Manufacturing} (2014)
\textsuperscript{254} Q110 [Dr Mughal]
Conclusions and recommendations

A new vision for our economy

1. In recognising the extent to which economic growth has failed to trickle down to many households and describing the causes of our poor productivity, the Government has provided a compelling argument for change. The Green Paper outlines deeply embedded weaknesses within the UK’s economy that have remained unresolved by successive governments. The UK’s headline economic success in recent decades has been felt by too few and its foundations are shallow. As a country, we have not invested enough in infrastructure or innovation, and our skills-levels remain poor despite significant spending. Too many people in too many parts of the country have not felt the benefits of growth. (Paragraph 16)

2. We strongly welcome and endorse the Prime Minister’s aspiration of “an economy that works for everyone”. The ultimate test of Government’s success in delivering this will be whether we see increased living standards across society and a reversal in the trend of widening gaps in the distribution of income and wealth. (Paragraph 17)

3. We agree with the Government’s vision that we should aspire towards an economy which is more productive and where the benefits of growth are felt more evenly throughout the UK. To this we would add that a further objective should be to ensure that the UK economy is fit to face the global challenges and opportunities of our age such as: the technological changes brought about through the fourth industrial revolution, and the challenges these will present for the labour market; changing demographics and an ageing population; and, the pressing need for decarbonisation. (Paragraph 18)

4. Successive governments over many decades have correctly identified long-term challenges and weaknesses within the UK’s economy on matters like poor productivity, skills deficiencies, inadequate investment on infrastructure and low spending on research and development. However, few administrations have had unqualified successes and many have spent huge amounts of taxpayers money in failing to address these weaknesses. While the Prime Minister’s rhetoric suggests an intention to approach this with a welcome and renewed vigour, the incremental proposals outlined in the Green Paper leave us sceptical about whether the fresh thinking or political will is present across Government to deliver the Prime Minister’s objectives. (Paragraph 19)

5. An explicit industrial strategy recognises that many Government policies inherently have an impact on the different sectors, nations and regions that comprise the UK’s economy. We have a choice as to whether these policies are implemented in an incoherent, ad hoc manner or work together toward a clear vision of the kind of economy we want. As the Prime Minister has recognised, an industrial strategy can provide a ‘practical and proactive’ framework for government intervention that can help address our economic weaknesses and ensure that our economy works for everyone. (Paragraph 29)
Principles for an effective industrial strategy

6. The Prime Minister’s rhetoric marks a significant shift away from that of previous Governments; consciously or unconsciously, it implies that the Government is willing to exchange headline economic growth for more evenly distributed and resilient growth. At a time when Government is already having problems in balancing the books, any decision to sacrifice some element of short-term economic growth for other objectives (with a longer-term return) will make that task more difficult. We would welcome clarity as to whether this is the right way to interpret her remarks. Success will only be achieved if policies are of a scale to match the Government’s ambition and clearly drive forward economic rebalancing. (Paragraph 37)

7. In its response to this Report, the Government should outline a set of clear, outcomes-focussed metrics that can be used to frame its goals and to measure progress in meeting these. We recommend that the Government should consider including metrics relating to the following:

- Improving in real-terms earnings per household and closing regional disparities;
- Reducing differential regional GDP per head between least and best performing nations and regions;
- Improving UK productivity relative to comparator economies and closing the gap with the G7 average;
- Improving UK Gross Domestic Expenditure on R&D relative to comparative OECD economies;
- Improving levels of UK investment in fixed capital relative to comparable OECD economies;
- Improving the UK’s position in international rankings on basic skills;
- Improving the UK’s position in international rankings on infrastructure;
- Ensuring emissions remain within Carbon Budgets and legal limits for air pollution;
- Closing the UK trade deficit; and,
- Improving the proportion of businesses which scale-up. (Paragraph 41)

8. We recommend that the Government publishes annual updates to its action plan outlining progress in delivering policies and setting out any new policies and how they align with the overall strategy. The Government should also create a single dashboard of metrics relating to industrial strategy on GOV.UK which should be updated as new statistics are published. (Paragraph 43)

9. Horizontal policies form the backbone of effective industrial policy. However, as the Government has recognised, they alone seem unlikely to deliver the Secretary of State’s larger ambition of getting to grips with “the problems and opportunities that we face over the next 10, 15 or 20 years.” (Paragraph 48)
10. Sectoral policies appear to have worked well for the automotive and aerospace industries. However, with regards to other sectors this approach has had, at best, mixed results. Furthermore, this approach appears to have the greatest risk of policy being built on the vested interests of big businesses and incumbents that are best equipped to lobby. Despite Government allowing sectors to self-identify, there is a risk that a sectoral approach encourages businesses to maintain rather than break down silos, and leads to policies designed to suit preferred industries at the expense of other sectors and the wider public interest. (Paragraph 54)

11. We recommend that Government reconsider giving sectoral strategies priority and instead focus on horizontal policies and specific ‘missions’ to meet UK-wide and local public policy challenges. (Paragraph 55)

12. In its response to this Report, the Government should set out the process by which it agreed to prioritise “deals” with the five sectors listed in the Industrial Strategy Green Paper, whether it held discussions with any other sectors about doing ‘deals’ and, if so, why those “deals” were not progressed at this time or referred to in the Green Paper. The Government also needs to clarify how it will evaluate future sectoral definitions, priorities and targets if it continues to pursue sectoral deals. (Paragraph 57)

13. Whereas a sector based approach is essentially another form of “picking winners”, a mission-based approach provides a means of articulating a positive economic vision and picking public policy challenges and allowing all sectors to put forward contributions to solving these. (Paragraph 63)

14. We recommend that specific support for industry be guided by a targeted ‘mission-based’ approach, channelling the Government’s support towards addressing the big challenges of the future. It is for Government to set those missions, in discussion with stakeholders. (Paragraph 64)

15. “Missions” need not be inconsistent with the Secretary of State’s vision of deals focussed on sectoral challenges. Rather, any such “deals” need a clear, time-bound goal. Furthermore, clear criteria are needed to decide which challenges are worth pursuing and which are not. Missions could provide a useful framework for setting those criteria. (Paragraph 65)

16. We strongly support the Prime Minister’s leadership in chairing the Cabinet Committee on the Economy and Industrial Strategy. It is also a positive indication of intent that the Secretary of State for Business, Energy and Industrial Strategy sits on more Cabinet Committees than any other Cabinet Minister, creating scope for a significant degree of coordination. However, we are conscious that ‘joined-up Government’ has remained an aspiration for many years that too often is unrealised in practice. The recent publication of the new Housing White Paper is a disappointing and early illustration that Whitehall does not appear to be joined up when it comes to industrial strategy. (Paragraph 71)

17. We recommend that the Government consider establishing a joint unit bringing together civil servants from BEIS, the Treasury, the Department for Communities and Local Government, and the Department for Education to provide an inter-departmental team to develop and implement the industrial strategy. (Paragraph 72)
18. Industrial strategy needs to provide a clear framework for how government will make policy choices. Trade-offs will need to be made between where Government spends its marginal pound—for instance, whether that is better invested in skills or in science and innovation or whether it is better invested in London or Leeds. We do not believe that the approach adopted in the Productivity Plan, which was essentially a wide-ranging assortment of loosely connected policies, many of which were pre-existing, is a good model to follow. (Paragraph 76)

19. The Government needs to clarify the relationship between its industrial strategy and its strategy for negotiating the UK’s future relationship with the EU. It is unfortunate that the recent White Paper on exiting the EU fails to do this in any meaningful way and reinforces a lack of coordination between the Government’s major challenge and its principal plank of business policy. It is logical for negotiating positions to be shaped and informed by the UK’s industrial strategy. (Paragraph 79)

20. It is clear that for a strategy to be genuinely long-term, Government will need to build a strong coalition of support for its objectives across economic actors. Failure to do so will critically undermine aspirations for a strategy which lasts longer than a single minister or Parliament. (Paragraph 82)

21. It is crucial that the Government’s industrial strategy sets out strong mechanisms for dialogue and collaboration with businesses (of all sizes) and unions, aimed at facilitating consensual agreement on future policy direction where appropriate. In responding to this Report, the Government should articulate how it plans to establish long-term stability within its industrial strategy. (Paragraph 84)

22. While it is to be expected that some of the UK’s largest employers and most successful companies are able to secure direct access to Ministers, the Government must ensure that industrial strategy does not become a vehicle for acquiescing to special pleading that protects and entrenches incumbents and disregards the need of less established or unified sectors, disrupters, or smaller businesses. (Paragraph 87)

23. We recommend that the Government improve the transparency of its engagement with business by publishing details of external meetings in a single, searchable database and extending publication to include all meetings that take place at Senior Civil Service level. (Paragraph 88)

24. A weakness of previous strategies is that they have largely engaged with top-tier companies but not engaged deeper into supply-chains. The Government’s industrial strategy needs to actively ensure that any policy interventions reach throughout the supply-chain. (Paragraph 90)

25. We recommend that the Government work with industry and local government to conduct a holistic review of the business services and support it offers with a view to simplifying access to advice on these in order to improve the ‘customer journey’. (Paragraph 93)

26. The Government needs to retain the flexibility to engage with businesses individually to encourage and support investment in the UK. For instance, we firmly welcome the fact that the Government was able to provide Nissan with assurances that
have helped ensure support for tens of thousands of jobs. But such support should be transparent and made within a clear and understandable policy framework. (Paragraph 95)

27. As has been the case with its efforts to support the steel industry, the Government should support industries it considers to be subject to anti-competitive pressures. But support should be in the context of helping industries that are facing challenging economic situations to adapt and thrive sustainably. Industrial strategy must not provide palliative care for failing and obsolete industries. Where industries are unsustainable, the Government’s priority should be to support individual workers, not to prop up particular companies. (Paragraph 96)

**Horizontal policy pillars**

28. We agree with the Secretary of State’s assessment that the UK needs to do more to commercialise its world-class R&D base and welcome commitments to do so. Catapult Centres are a promising model for public–private collaboration and we urge Government to allow them time to grow and avoid unnecessary tinkering. We also welcome evidence that universities are increasing their focus on commercialising their research; this should continue to be encouraged and supported. (Paragraph 99)

29. We are disappointed that the Government’s response to our Report on the Productivity Plan did not accept our recommendation to set a target of increasing public and private R&D investment to 3 per cent of GDP. (Paragraph 102)

30. **We repeat our previous recommendation that the Government should set a target to increase R&D investment to 3 per cent of GDP and implement policies to achieve it.** (Paragraph 103)

31. As part of its review of the tax environment for R&D, the Government should not shy away from ambitious measures to ensure additionality. (Paragraph 106)

32. **In line with the Secretary of State’s stated aim to support disruptors and economic innovation, we recommend that the Government review with industry whether additional steps are needed to provide regulatory certainty for emerging business models.** (Paragraph 111)

33. A skilled workforce is an essential foundation of economic success. Given the weaknesses identified by the Government in the UK’s skills base, the proposals contained in the industrial strategy Green Paper leave much to be desired. After six months in development we expected more than a disappointing combination of re-announcements, continuations of existing policy, and vague aspirations. It is deeply disappointing that the Green Paper fails to outline any detailed proposals for discussion in relation to encouraging the uptake of STEM subjects, and improving the skills of those already of working age. These will need to be addressed far more comprehensively in the White Paper. We welcome commitment to a proper system of technical education, linked to local needs, but it is unclear how this actually goes beyond proposals contained in the previous Productivity Plan. The Government needs to set out more detail about how it will achieve parity of esteem between vocational and academic training in practice. (Paragraph 115)
34. **We recommend that the Government consider the potential for greater devolution of responsibility and funding for skills to local authorities and Local Enterprise Partnerships, who are well placed to work to identify regional needs and design appropriate solutions.** (Paragraph 117)

35. In the context of negotiations over free-movement as part of withdrawal from the EU, Government must ensure that businesses continue to be able to access the skills they need. In its response to our Report, the Government should provide further clarity on how it intends to do this. (Paragraph 121)

36. **We recommend that the Government exclude university students from immigration totals and promote high skilled migration to the UK on an equal “who contributes most” basis to people wishing to invest and innovate in the UK.** (Paragraph 122)

37. We presume that the Government has always prioritised “the highest value-for-money projects”. Given this, we would welcome clarity on how its approach will differ in the future to better support rebalancing. (Paragraph 126)

38. The decision not to place the National Infrastructure Commission on a statutory footing risks creating the impression that the Government is not backing up its aspiration for a long-term policy framework with action that will help embed that. (Paragraph 128)

39. We are surprised that the National Infrastructure Commission gets little prominence in the industrial strategy and it is unclear how the questions in the Green Paper are intended to complement the Commission's own call for evidence. For example, has the Commission been asked to prioritise rebalancing in its assessment of the country’s infrastructure requirements? We would welcome clarification from the Government. (Paragraph 129)

40. The problem of impatient capital and the UK’s poor track-record on scale-up have been subject to a number of reviews in recent years. We welcome the fact that Government is taking this issue seriously and look forward to seeing the review followed by meaningful action. We will also continue to consider this issue as part of our inquiry into Corporate Governance and a new inquiry into Scale-Up. (Paragraph 131)

41. Evidence on the impact of Growth Hubs is mixed. In its response to this Report, Government should set out how it intends to evaluate the impact of current funding in order to determine what needs to be done to support Growth Hubs to provide a better service in the future. (Paragraph 133)

42. **Fiscal levers can play a key role in shaping business behaviour. We recommend that Government commission an independent review bringing together broad representation to consider whether taxation levers can better be used to boost investment in physical and human capital, research and innovation.** (Paragraph 136)

43. **We recommend that the Government conduct a fundamental review of the outdated structure of the business rates system, given that it acts as a disincentive to investment regardless of who is responsible for setting the overall rate.** (Paragraph 138)
44. We welcome the fact that the Government is considering opportunities to better utilise public procurement to maximise economic opportunity for UK firms, and it should make greater use of flexibility in existing state aid rules prior to our departure from the European Union. The Government should also consider the opportunities to further boost procurement from within the UK as part of its negotiating strategy for withdrawal from the EU. (Paragraph 140)

45. We welcome the review of the Small Business Research Initiative that the Government has commissioned; we hope this will be ambitious in its recommendations and that the Government will increase the scale of the scheme and better embed it across Whitehall. (Paragraph 142)

46. Given the Prime Minister’s previous comments about foreign takeovers, the Government needs to provide much greater clarity and certainty as to what steps it intends to take to intervene in foreign takeover deals and in what circumstances. (Paragraph 150)

47. We recommend that the Government takes steps to ensure it has the power to retain IP benefits in the UK in the event of a foreign takeover where a business has been supported in developing new IP through taking advantage of taxpayer funding or tax-incentives. At the very least, it should ensure that any transfer of IP delivers a substantial return for taxpayers. This could be done, for instance, by placing constraints on access to funding and incentives. The Government should also develop mechanisms to clawback any tax relief or funding should tax-payer subsidised IP be transferred abroad. (Paragraph 152)

48. While we welcome the industrial strategy’s support for energy innovators, taking advantage of the economic opportunities presented by decarbonisation also means ensuring the UK continues to be seen as a world-leader in the transition to a low-carbon economy. In this context, we trust that the Government will publish its Emissions Reduction Plan by the end of March 2017, as indicated to us by the Minister of State for Climate Change and Industry. The Government needs to ensure that the Emissions Reduction Plan and industrial strategy are coherent and consistent, with commitments in the industrial strategy to actively support delivery of current and future carbon budgets. (Paragraph 156)

Rebalancing our economy

49. The Committee welcomes the positive signs that the Government will look to work closely in collaboration with the UK’s various national, local and regional governments in developing its industrial strategy. Where additional powers are devolved, the Government needs to ensure that appropriate funding is also devolved. (Paragraph 162)

50. While variations in perceived performance of Local Enterprise Partnerships are to be expected—that is part and parcel of devolution—the Government has a role in supporting and multiplying best practice. Given the prevalence of concerns and low awareness of LEPs, as well as fiscal constraints, the Government should review LEPs
to ensure that needless duplication is avoided, best practice is shared, and value for money is secured. This should include ensuring governance and accountability frameworks are fit for purpose. (Paragraph 163)

51. The Government needs to provide clarity on the respective roles and responsibilities between national, local and regional institutions. Failure to do so will lead to unnecessary complexity and confusion for business and reduce accountability to the electorate. In partnership with business representatives, local government and the devolved administrations, the Government should consider whether any further steps are desirable to facilitate businesses in understanding and navigating different tiers of devolution. While many services may best be designed at a local level, the Government needs to ensure that it avoids creating barriers to cooperation between local institutions or inadvertently introducing perverse incentives that lead to needless and inefficient duplication of services. (Paragraph 167)

52. We recommend that the Government set out a clear plan to close per head spending gap on infrastructure, R&D and education between London and the rest of England. (Paragraph 170)

53. While the Government is experimenting more with fiscal devolution, such as the planned devolution of powers to set business rates, it is notable that the Industrial Strategy Green Paper is broadly silent on the potential for further fiscal devolution. (Paragraph 172)

54. While recognising the importance of the services sector, and the UK’s comparative economic advantage, supporting industries which produce goods, technology, and innovation, will help boost productivity and create high-quality jobs. We welcome signs that the Government recognises the value of rebalancing our economy in this way. (Paragraph 177)
Annex: Note of the Committee’s visit to Sweden, 27–29 November 2016

This note provides a record of the visit to Sweden undertaken by members of the Business, Energy and Industrial Strategy Committee. The purpose of the visit was to hear first-hand how the Swedish Government developed its recent ‘Smart Industry’ strategy, and to learn about Sweden’s model of corporate governance and industrial relations.

Members in attendance: Iain Wright MP (Chair), Amanda Milling MP, Peter Kyle MP, Michelle Thomson MP, Chris White MP

GKN Aerospace Engine Systems

- Hannes Carl Borg, Public Affairs GKN Sweden
- Chris Saunders, Public Affairs GKN UK

GKN had operations in both Sweden and the UK and provided its views on differences and similarities in industrial policy in both countries. The Committee discussed the importance of industrial policy in supporting innovation, and the importance of skills to GKN’s sector.

Like the UK, Sweden struggled with a skills gap and was concerned about the increasing global competitiveness of R&D. In Sweden, there was greater stability to the innovation landscape than in the UK because Government agencies were more operationally independent.

Previous Swedish strategies focussed more on specific industries but the current one is focussed more on social “challenges”. This was seen as a positive step that gave a stronger sense of direction. Focussing on societal challenges had helped create political consensus that should bring greater stability to the strategy.

The UK was seen as having a fear of picking winners, for instance it didn’t have a long-term strategy for additive manufacturing. This was worrying. It was recognised that providing support for particular innovations and sectors carried risk but that was something which Government was well placed to do whereas an individual company might struggle.

In Sweden, there was a clear and valued vision but limited funding to back it up. In the UK, Government still has significant funding at its disposal but needed a clearer vision and the commitment to follow it.

Ministry of Enterprise and Innovation

- Eva Lindström, State Secretary to the Minister for Enterprise & Innovation

The current Government was formed in 2014, and prioritised an industrial strategy because it felt that the industrial (manufacturing) sector had been neglected. Particular concerns included skills and innovation support.
One motivation for the new industrial strategy was the belief that industry needed to be seen as “the engine to solve society’s problems.” Industrial strategy was “not just about what’s happening to our industry, it’s about what’s happening to our society.”

To support implementation of the new industrial strategy, the Government intended to publish updated action plans twice a year that include new measures as well as a rolling programme of work.

Ministers across departments had strong ownership. For instance, ministers from multiple departments met stakeholders together and ministers had set aside a lot of time to directly lead workshops with business.

It was felt that one “advantage” of the Swedish strategy is that it didn’t pick winning sectors but focuses on the real economic and social challenges Sweden faces.

**Business Roundtable**

- **Aidan Liddle**, Deputy Head of Mission, British Embassy Stockholm

A lunch was hosted by the British Embassy with a range of Swedish business representatives. Committee members informally discussed a range of themes, including how to design effective industrial strategy, the role of automation and digitalisation, and the risks of protectionism.

**Mannheimer Swartling**

- **Adam Green**, Partner and Head of Mergers and Acquisitions

Sweden anecdotally had more multi-national companies per capita than any other country in the world and more “unicorn” companies in the tech sector than any country except the US.

Sweden had a small domestic market so it was widely recognised that companies had to export to grow and succeed. The success of some major Swedish brands had given entrepreneurs confidence to succeed.

In Sweden there was a tradition of companies being run by sectoral experts—whereas there was a perception that in the UK companies are overly financialised and run by finance officers.

Mergers and acquisitions was perceived to be “the back end of investment”. “You either do it for dividends or to sell on a start-up if you are investing in the hope of a longer-term pay off.” Investing in start-ups was “a different ecosystem with different expectations” from investing in listed shares.

Sweden rebounded so quickly from the 2008 financial crisis because it had learned lessons from the crisis in the early 1990s.

Sweden had always had a relatively collectivist culture—“we are a small country; we recognise we are all in the same boat.”
Swedish Confederation of Industry & Federation of Technology Companies

- **Tobias Krantz**, Head of Education, Research and Innovation (SCI)
- **Göran Norén**, Head of Industrial Affairs (SCI)
- **Jonas Berggren**, Head of International Affairs (SCI)
- **Jennie Cato**, Director Trade Promotion Policy (FSEI)
- **Cecilia Warrol**, R&D, Programme Director Production 2030 (FSEI)

In Sweden there was a belief in codetermination between business and the unions. While the relationship was inevitably not always easy, in key areas such as education, skills and innovation, there was good cooperation and agreement.

Sweden needed to export to maintain its standard of living. Unions recognised this and so accepted job losses that accompanied productivity increases, but also ensured a strong social safety net was maintained. While those in the manufacturing sector understood the need to stay competitive—incents were less strong for domestically focussed unions.

The Confederation welcomed provisions in Sweden’s new Research and Innovation Bill to incentivise businesses and universities to work more closely together. The “innovation premium” was designed to reward universities for knowledge transfer and commercialisation activities.

The new industrial strategy was welcome and broad enough to accommodate different sectoral needs; it was also hoped that it would lead to better cross-government coordination. One particular challenge was that regional government was not necessarily very engaged with industrial strategy.

Vinnova

- **Ulf Holmgren**, Director and head of industrial technologies and innovation management division
- **Margareta Groth**, Head of Industrial Technologies Department

Vinnova employed around 200 staff, the vast majority in Stockholm, but it also had a small office in Brussels and a member of staff in Silicon Valley.

Swedish agencies had a significant degree of autonomy—Vinnova had a large amount of freedom around how it operates. In its experience, this was quite different to similar agencies elsewhere in Europe, where Government expressed a stronger degree of control. By being outside of Government structures, Vinnova believed they were better able to innovate and be more flexible. They were accountable to Government which set their overarching budget and objectives.

Sweden’s approach to innovation funding had evolved in recent years. In 2008, Government proposed 24 strategic research areas that were picked “top-down”—four were given direct
funding and 20 on the basis of open-competition. This approach was then modified in 2011/12 when Vinnova developed a number of ‘strategic innovation areas’ which looked less at sectors and more at cross-cutting challenges.

The most recent stage of the evolution in 2016 was the introduction of “innovation partnerships” which aimed to fund bottom-up collaborations that would help companies run faster than their competitors in emerging economies. This approach was not sectoral but was based on Vinnova reviewing bids produced from industry. It built on the concept that innovation was stimulated when sectoral boundaries are crossed: “If I want a new idea, I don’t invite ten people like myself into a room.” Under the strategic innovation partnerships programme, Vinnova had a set budget and a number of strategic challenges were set by Government, but “we don’t define what is important, others do.”

The OECD had often said that Sweden should be more coordinated and top-down, but Vinnova believed that the bottom-up approach complemented Swedish culture.

**IF Metall**

- **Ola Asplund**, Senior Advisor to the President of IF Metall
- **Erica Sjölander**, Head of the Research Department.
- **Aleksandar Zuza**, Research Officer

Collective bargaining played a central role to Swedish wage-setting. The benchmarks for national wage increases in the manufacturing sector were increases in competitiveness and productivity. This had led to a 60% real terms wage increase in the past 20 years. It also meant that unions were committed to improving competitiveness and productivity, even recognising that this may lead to job losses. The key was to ensure employees who were made redundant had access to a strong social safety net and the ability to retrain and reskill—“we don’t protect the ship we protect the sailors”.

The relationship between business and unions in the 1970s and 1980s was more akin to the oppositional relationship that exists in the UK today. However, this changed following the 1990s economic crisis in Sweden, and there was now a strong “social trust” between business, government and unions.

**AstraZeneca**

- **Jan-Olof Jacke**, CEO, Astra Zeneca AB
- **Jacob Lund**, Director of External Communications

Industrial strategy should not be about picking winners but about “creating attractive conditions for businesses to grow.” For AstraZeneca in Sweden that meant a better life sciences ecosystem, including more growing SMEs, and greater collaboration. Businesses in the life sciences sector benefited from the fact they trusted successive governments would continue to provide support regardless of who was in power. AstraZeneca benefited from “a commitment to the sector” rather than from a specific strategy.
Sweden was an open economy, FDI and foreign ownership was key to help support growth and to avoiding protectionism that would hinder Swedish companies in making acquisitions overseas.

The corporation tax rate in the UK was important for investment, but it is less important than having a skills and innovation environment where businesses could create value and make great products.

The real challenge for industrial strategy—in Sweden and in the UK—was in translating a positive vision into concrete actions.
Draft Report (Industrial Strategy: First Review), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 177 read and agreed to.

Summary agreed to.

Resolved, That the Report be the Second Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

Written evidence was ordered to be reported to the House for publishing with the Report (in addition to that ordered to be reported for publishing on 11, 25, 27 October, 1, 8, 22 November and 10 January).

[Adjourned till Wednesday 22 February at 9.00 am]
Witnesses

The following witnesses gave evidence. Transcripts can be viewed on the inquiry publications page of the Committee’s website.

Tuesday 11 October 2016

Rt Hon Sir Vince Cable
Rt Hon George Osborne MP and Rt Hon Lord Heseltine

Thursday 27 October 2016

Dr Hamid Mughal, Director of Global Manufacturing, Rolls-Royce and Professor David Greenwood, Warwick Manufacturing Group

Councillor Bob Sleigh, leader of Solihull Metropolitan Borough Council and Chair, West Midlands Combined Authority, Matthew Rhodes, board member of the Greater Birmingham and Solihull LEP, and Jonathan Browning, Chair, Coventry and Warwickshire LEP

Andy Palmer, Chief Executive, Aston Martin, David Bailey, Professor of Industrial Strategy, Aston Business School, Rachel Eade, Automotive Supply Chain Specialist, and Tony Burke, Unite Assistant General Secretary for Manufacturing

Tuesday 8 November 2016

Kevin Baughan, Chief Development Officer, Innovate UK, Dr Celia Caulcott, Vice-Provost (Enterprise), University College London, Professor John Latham, Chair of University Alliance & Vice-Chancellor of Coventry University, and Dr Sarah Main, Director, Campaign for Science & Engineering

Stephen Ibbotson, Director of Business, Institute of Chartered Accountants in England and Wales, Stephen Tarr, Managing Director (Projects), Balfour Beatty, and Ben Wilmott, Head of Public Policy, Chartered Institute of Personnel and Development

Tuesday 22 November 2016

Alex Brummer, City Editor, Daily Mail, Lee Hopley, Chief Economist, EEF, Paul Kahn, President, Airbus UK, Rhian Kelly, Director for Infrastructure, CBI, Mark Littlewood, Director General, Institute of Economic Affairs, Mariana Mazzucato, RM Phillips Professorship in the Economics of Innovation, University of Sussex, Paul Nowak, Deputy General Secretary, TUC, Stephen Pattison, Vice-President Public Affairs, ARM Holdings, Ashley Shackleton, Head of Public Affairs, British Chambers of Commerce, and Simon Walker, Director General, Institute of Directors
Thursday 8 December 2016

Edward Twiddy, Chief Innovations Officer, Atom Bank, Jane Mee, General Counsel, Hitachi Rail Europe, and Dr Jennifer Thompson, Head of Partnerships and Engagement, Durham University

James Ramsbotham, Chief Executive, North East England Chamber of Commerce, Graham Robb, Board Member of the South Tees Development Corporation and Chair of North East Institute of Directors, and John Elliott, Chairman, Ebac Ltd

Nigel Foster, Director of Strategy, Transport for the North, Councillor Iain Malcolm, North East Combined Authority, Andrew Lewis, Managing Director, Tees Valley Combined Authority, and Anna Round, Senior Research Fellow, IPPR North

Thursday 15 December 2016

Rt Hon Lord Mandelson
Published written evidence

The following written evidence was received and can be viewed on the inquiry publications page of the Committee’s website.

ISG numbers are generated by the evidence processing system and so may not be complete.

1. ABB (ISG0051)
2. Aberdeen & Grampian Chamber of Commerce (ISG0107)
3. ABHI (ISG0083)
4. ACAS (ISG0168)
5. ADS Group (ISG0095)
6. Aerospace Technology Institute (ISG0037)
7. AIRTO Ltd (Association of Innovation, Research & Technology Organisations) (ISG0034)
8. Aldersgate Group (ISG0138)
9. Alliance for Intellectual Property (ISG0106)
10. Angel Trains (ISG0058)
11. ARM Ltd (ISG0005)
12. Arqiva (ISG0080)
13. Arts Council England (ISG0191)
14. Association of Convenience Stores (ISG0165)
15. Association of Independent Professionals and Self-Employed (IPSE) (ISG0122)
16. Balfour Beatty (ISG0164)
17. BFI (ISG0177)
18. BioIndustry Association (ISG0078)
19. British Aggregates Association (ISG0162)
20. British Ceramic Confederation (ISG0030)
21. British Chamber of Commerce (ISG0181)
22. British Coatings Federation (ISG0009)
23. British Glass (ISG0021)
24. British Hospitality Association (ISG0073)
25. British Marine (ISG0141)
26. British Plastics Federation (ISG0105)
27. British Property Federation (ISG0042)
28. British Standards Institution (ISG0113)
29. British Woodworking Federation (ISG0114)
30. BT (ISG0153)
31. Buckinghamshire Thames Valley LEP (ISG0092)
32. Building Engineering Services Association (ISG0169)
33. Business in the Community (ISG0084)
34 Campaign for Science and Engineering (ISG0158)
35 Cancer Research UK (ISG0099)
36 Carbon Capture and Storage Association (ISG0119)
37 Centre for Competition Policy (ISG0125)
38 Centre for Local Economic Strategies (ISG0081)
39 Centre for Process Innovation (ISG0033)
40 Centre for Urban and Regional Development Studies (CURDS) (ISG0185)
41 CF Fertilisers (ISG0082)
42 Chemical Industries Association (ISG0103)
43 Chief Economic Development Officers Society (CEDOS) (ISG0056)
44 CIPD (ISG0064)
45 CityREDI (ISG0188)
46 Civil Engineering Contractors Association (ISG0008)
47 CoallMnP (ISG0101)
48 Commercial Broadcasters Association (ISG0167)
49 Competition and Markets Authority (ISG0128)
50 Confederation of British Industry (ISG0133)
51 Confederation of Paper Industries (ISG0031)
52 Construction Industry Training Board (ISG0155)
53 Construction Products Association (ISG0024)
54 Core Cities (ISG0186)
55 Cornwall Council (ISG0063)
56 Creative England (ISG0175)
57 Creative Industries Federation (ISG0137)
58 Cumbria County Council (ISG0094)
59 Dell EMC (ISG0043)
60 Department for Business, Energy and Industrial Strategy (ISG0189)
61 Dr Jian Tong (ISG0116)
62 Dr Richard Worswick (ISG0018)
63 Dr SIMON LEE (ISG0124)
64 East Midlands Chamber (Derbyshire, Nottinghamshire, Leicestershire) (ISG0039)
65 EDF Energy (ISG0060)
66 EEF – the manufacturers’ organisation (ISG0067)
67 Energy & Utility Skills Group (ISG0088)
68 Energy Intensive Users Group (ISG0120)
69 Energy Technologies Institute (ISG0126)
70 Engineering Professors’ Council (ISG0047)
71 England’s Economic Heartland Strategic Alliance (ISG0097)
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The reference number of the Government’s response to each Report is printed in brackets after the HC printing number.

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Second Report The Government’s Productivity Plan HC 466 (HC 931)
First Special Report Competition in the postal services sector and the Universal Service Obligation: Responses to the Committee’s Ninth Report of Session 2014–15 HC 476
Second Special Report Education, skills and productivity: commissioned research HC 565
Third Special Report The UK steel industry: Government Response to the crisis: Response to the Committee’s First Report of Session 2015–16 HC 861

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First Report Careers education, information, advice and guidance HC 205
Second Report The Digital Economy HC 87 (HC 930)
Third Report Employment practices at Sports Direct HC 219
Fourth Report BHS HC 54
Fifth Report The use of UK-manufactured arms in Yemen HC 679
### List of Reports from the Business, Energy and Industrial Strategy Committee during the current Parliament

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The reference number of the Government’s response to each Report is printed in brackets after the HC printing number.

#### Session 2016–17

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